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Notes

THE ACT OF STATE DOCTRINE AND *ALLIED BANK*

I. INTRODUCTION

Since the early 1970's, United States banks have loaned billions of dollars to developing countries considered creditworthy based on their historic growth rates and vast untapped natural resources.¹ In 1980-1981, however, many of these borrower countries became unable to service their external debt as a result of the coincidence of the worldwide recession, depressed export markets, disinflation, and lower oil prices.²

The enormity of United States banks' involvement in international loan transactions accounted for the grave concern that arose in the

1. See Eskridge, *Les Jeux Sont Faits: Structural Origins of the International Debt Problem*, 25 VA. J. INT'L L. 281, 293-94 (1985). Professor Eskridge explains that the largest total bank loans were made to Latin American countries. *Id.* at 282. As of 1983, the leading borrowers in Latin America were Brazil, Mexico, Argentina, and Venezuela; exposure of eight leading United States banks in loans to these countries, as of December 31, 1983, is shown below:

Bank	Millions of Dollars in Loans				Loans as % of Bank's Capital
	Argentina	Brazil	Mexico	Venezuela	
Citicorp	1090	4700	2900	1500	154.3
Bank America	300	2484	2741	1614	116.7
Mf'rs Hanover	1321	2130	1915	1084	200.3
Chase Manhattan	775	2560	1553	1226	136.5
J.P. Morgan	741	1785	1174	464	102.9
Chemical	370	1276	1414	776	136.0
Bankers Trust	230	743	1286	436	119.4
Continental Ill.	401	476	699	436	83.9

Id. at 293 n.23 (citing Latin American Times, Apr. 16, 1984, at 8). See also Comment, *On Third World Debt*, 25 HARV. INT'L L.J. 83, 88-89 (1984). The unprecedented lending to lesser developed countries was made possible by a surge of dollar deposits in United States banks by the Organization of Petroleum Exporting Countries (OPEC) following OPEC's four-fold oil price increases in 1973. *Id.* at 88. The banks, in turn, loaned money to developing countries, some of which needed money to pay "spectacular" oil bills and all of which needed money to stimulate their domestic economies. *Id.* at 90. See also Mendez, *Recent Trends in Commercial Bank Lending to LDCs: Part of the Problem or Part of the Solution*, 8 YALE J. WORLD PUB. ORD. 173, 176-81 (1982). Prior to 1973, developing countries obtained needed capital from public sources; credit extended by multi-lateral financing agencies such as the International Monetary Fund and the International Bank for Reconstruction and Development (the World Bank), government loans, and the sale of government bonds were the main credit sources. *Id.* at 176. However, since 1973, with the dramatic increase in loans from commercial banks, about two-thirds of the debt of the developing world is owed to private creditors. *A Nightmare of Debt: A Survey of International Banking*, ECONOMIST, Mar. 20, 1982, at 99.

2. See Eskridge, *supra* note 1, at 282-84.

banking community when, in 1981, the Costa Rican government issued directives temporarily prohibiting Costa Rican banks from repaying external debts in foreign currency.³ As a result of the Costa Rican directives, two banking syndicates⁴ that had loaned money to Costa Rican banks brought suit in the United States to enforce the terms of the loan agreements.⁵

These cases turned on the issue of whether the act of state doctrine⁶

3. For a discussion of the Costa Rican directives, see *infra* note 122.

4. Banking syndicates, or associations of banks, were often formed to finance loans to foreign governments and their instrumentalities. See Clarke & Farrar, *Rights and Duties of Managing and Agent Banks in Syndicated Loans to Government Borrowers*, 1982 U. ILL. L. REV. 229; Semkow, *Syndicating and Rescheduling International Financial Transactions: A Survey of the Legal Issues Encountered by Commercial Banks*, 18 INT'L LAW. 869 (1984). See also *infra* note 124.

5. *Libra Bank Ltd. v. Banco Nacional de Costa Rica, S.A.*, 570 F. Supp. 870 (S.D.N.Y. 1983); *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 566 F. Supp. 1440 (S.D.N.Y. 1983), *rev'd*, 757 F.2d 516 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985).

For a discussion of the *Libra* case, see *infra* note 126. For a discussion of the *Allied* case, see *infra* notes 124-57 and accompanying text.

6. The act of state doctrine prohibits review of acts of a foreign sovereign by United States courts. See *Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398, 401 (1964). Although the doctrine is often confused with sovereign immunity, the two doctrines are distinct. See Ebenroth & Teitz, *Winning (or Losing) by Default: The Act of State Doctrine, Sovereign Immunity and Comity in International Business Transactions*, 19 INT'L LAW. 225, 230-31 (1985). Sovereign immunity focuses on whether the foreign sovereign may be a party to the suit, not on the acts of a foreign sovereign. See Comment, *Applying an Amorphous Doctrine Wisely: The Viability of the Act of State Doctrine After the Foreign Sovereign Immunities Act*, 18 TEX. INT'L L.J. 547, 564 (1983). Historically, foreign sovereign states were granted absolute immunity from the jurisdiction of United States courts. *Id.* at 548-49. The concept of absolute immunity, however, was superseded in the United States courts by a restrictive theory of sovereign immunity under which a court could exercise jurisdiction over a sovereign state acting in a private or commercial capacity. *Id.* at 549-50.

In 1976, Congress enacted the Foreign Sovereign Immunities Act (FSIA), which codified the restrictive theory. Foreign Sovereign Immunities Act, Pub. L. No. 94-583, 90 Stat. 2892 (1976) (codified as amended at 28 U.S.C. §§ 1602-1611 (1982)). The FSIA "provided a statutory means for obtaining service upon, and in personam jurisdiction over, a foreign state; and attempted to provide the judgment creditor a remedy should the foreign state fail to satisfy a final judgment." Comment, *supra*, at 550-51 (footnote omitted). In part, the FSIA declares that a foreign state is not immune from jurisdiction in any of the following circumstances: (1) where the foreign state has explicitly or implicitly waived its immunity; (2) where the cause of action is based on a commercial activity carried on by the foreign state; and (3) where property, present in the United States by reason of the foreign state's commercial activities, was taken in violation of international law. 28 U.S.C. §§ 1605(a)(1), (2), (3) (1982).

Where a United States bank enters into a loan agreement with a foreign sovereign state or one of its instrumentalities, the bank will typically require the foreign borrower to waive immunity. See Comment, *supra* note 1, at 100-04. If the borrower subsequently defaults, the borrower will not be able to raise sovereign immunity as a defense to jurisdiction. See *id.* at 105-07. If the default is compelled by a governmental act restricting external debt repayments, a court, notwithstanding its jurisdiction under the FSIA, may recognize the act of the

requires United States courts to recognize the validity of the Costa Rican directives.⁷ The act of state doctrine is a judicial doctrine whereby a United States court, notwithstanding its jurisdiction over a case, will not question the validity of an act of a foreign sovereign state done within that state's territory.⁸ One of these cases, *Allied Bank International v. Banco Credito Agricola de Cartago*,⁹ reached the Court of Appeals for the Second Circuit, which initially did not address the applicability of the act of state doctrine,¹⁰ and then, on rehearing, vacated its earlier decision and found the doctrine inapplicable.¹¹

The *Allied* case brings to the forefront the problems which result in applying traditional act of state analyses to acts by debtor countries affecting intangible property such as a bank debt. This note will examine the act of state doctrine and the rationales set forth by the Supreme Court that justify application of the doctrine. The note will also describe the application of the doctrine to intangible property by lower

defaulting sovereign borrower under the act of state doctrine. Cf. *Callejo v. Bancomer, S.A.*, 764 F.2d 1101 (5th Cir. 1985). *Callejo* involved a suit brought by United States citizens who held certificates of deposit issued by a Mexican bank. *Id.* at 1105. In 1982, the Mexican government issued exchange controls that compelled the Mexican bank to pay the certificate holders substantially less than the face value of the certificates upon maturity. *Id.* at 1106. When the holders sued, the Mexican banks asserted the defense of sovereign immunity. *Id.* Although the Mexican banks were nationalized, the court did not find the banks immune from jurisdiction under the FSIA. *Id.* at 1106-12. The certificate holders thus met the jurisdictional requirements for bringing suit against the Mexican banks; however, they did not prevail because the court held that the act of state doctrine applied to the Mexican government's act of imposing exchange controls. *Id.* at 1125. For a further discussion of the *Callejo* case, see *infra* notes 88-95 and accompanying text.

Further discussion of sovereign immunity and the FSIA is beyond the scope of this note. For an analysis of the relationship of the act of state doctrine to the doctrine of sovereign immunity, see generally Comment, *supra*.

7. *Libra Bank Ltd. v. Banco Nacional de Costa Rica, S.A.*, 570 F. Supp. 870, 877-84 (S.D.N.Y. 1983); *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 566 F. Supp. 1440, 1443-44 (S.D.N.Y. 1983), *rev'd*, 757 F.2d 516 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985).

8. See *Banco Nacional de Cuba v. Sabbatino*, 376 U.S. 398, 428 (1964). For a recent, comprehensive overview of the act of state doctrine see Bazylar, *Abolishing the Act of State Doctrine*, 134 U. PA. L. REV. 325 (1985).

9. 566 F. Supp. 1440 (S.D.N.Y. 1983), *rev'd*, 757 F.2d 516 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985).

10. *Allied Bank Int'l v. Banco Credito Agricola de Cartago (Allied I)*, No. 83-7714 (2d Cir. Apr. 23, 1984) [reprinted in 23 INT'L LEGAL MATERIALS 742, 746 (1984)], *withdrawn and vacated*, 757 F.2d 516 (2d Cir.) (*Allied II*), *cert. dismissed*, 106 S. Ct. 30 (1985). After the Second Circuit granted a rehearing (*Allied II*), the *Allied I* decision, which initially appeared in the advance sheets of the *Federal Reporter*, 733 F.2d 23, was withdrawn from the bound volume. Subsequent citations to *Allied I* will be to its reprinting in *International Legal Materials*. For a discussion of *Allied I*, see *infra* notes 127-38 and accompanying text.

11. *Allied Bank Int'l v. Banco Credito Agricola de Cartago (Allied II)*, 757 F.2d 516, 519-21 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985). For a discussion of *Allied II*, see *infra* notes 139-57 and accompanying text.

courts, which have set forth several inconsistent tests for determining whether the intangible property at issue falls within the doctrine. Finally, this note will criticize the Second Circuit's decision in the *Allied* case, in which the issue of whether to apply the act of state doctrine turned on a tenuous analysis of the "situs" of the Costa Rican bank debt. In light of the fact that the act of state doctrine was developed with respect to sovereign acts affecting tangible property within the foreign sovereign's dominion, this note will suggest that in cases involving intangible property, a court should not engage in the impossible task of locating the intangible property, but rather should apply the doctrine based on its policy justifications as set forth by the Supreme Court.¹²

12. In addition to the act of state doctrine, the International Monetary Fund Articles of Agreement (Bretton Woods Agreement) arguably controls litigation questioning a sovereign state's currency controls that affect international loan transactions. See, e.g., Gold, *Exchange Control: Act of State, Public Policy, the IMF's Articles of Agreement, and Other Complications*, 7 HOUS. J. INT'L L. 13 (1984). While an extensive discussion of the International Monetary Fund (IMF) is beyond the scope of this note, a brief explanation of the IMF and its potential application to international loan transactions follows.

In 1944, 44 countries, including the United States, established the International Monetary Fund. J. PIPPENGER, *FUNDAMENTALS OF INTERNATIONAL FINANCE* 138, 141 (1984). Member countries contribute money to the IMF for the primary purpose of aiding countries with balance of payment deficits, i.e., where payments made for imports are below payments received for exports. See 2 P. WOOD, *LAW AND PRACTICE OF INTERNATIONAL FINANCE* § 4.14[1][a] (1986). Where a member country is in payment difficulties, the IMF can, as a lender of last resort and on a limited basis, provide currency to restore a country's credit. See *id.* Additionally, "the Fund has the necessary diplomatic power to insist upon the adoption of fiscal reforms and other austerity programmes as a condition of its assistance . . . [thereby encouraging] private lenders to make up for the limited resources of the Fund by restoring credit to the member [country] concerned" *Id.* See also Robichek, *The International Monetary Fund: An Arbiter in the Debt Restructuring Process*, 23 COLUM. J. TRANSNAT'L L. 143 (1984).

Article VIII, § 2(b), of the Bretton Woods Agreement addresses the extra-territorial effect of exchange control regulations that a member country maintains consistently with the Bretton Woods Agreement: "Exchange contracts which involve the currency of any member and which are contrary to the exchange control regulations of that member maintained or imposed consistently with this Agreement shall be unenforceable in the territories of any member." International Monetary Fund Articles of Agreement, Dec. 27, 1945, art. VIII, § 2(b), 60 Stat. 1401, T.I.A.S. No. 1502, 2 U.N.T.S. 39, amended by 20 U.S.T. 2775, T.I.A.S. No. 6748, 726 U.N.T.S. 266 (May 31, 1968), amended by 29 U.S.T. 2203, T.I.A.S. No. 8937, — U.N.T.S. — (Apr. 30, 1978) (codified by reference at 22 U.S.C. § 286h (1982)). In essence, this section of the Agreement provides that exchange control regulations including, perhaps, directives such as those issued by Costa Rica, may invalidate "exchange contracts" extraterritorially. See Ebenroth & Teitz, *supra* note 6, at 247-48. The crucial question where a member country invokes this provision to invalidate an international loan agreement is whether the loan agreement may be characterized as an "exchange contract." *Id.* at 248.

Libra Bank Ltd. v. Banco Nacional de Costa Rica illustrates how this provision of the Bretton Woods Agreement is invoked. 570 F. Supp. 870, 896-902 (S.D.N.Y. 1983). In *Libra*, a British banking syndicate sued a Costa Rican bank in the United States when the Costa Rican Bank defaulted on a loan following the issu-

II. THE ACT OF STATE DOCTRINE

In 1897, the act of state doctrine was first articulated by the United States Supreme Court in *Underhill v. Hernandez*,¹³ a case in which a United States citizen sued the revolutionary military governor of Venezuela for unlawful confinement and assault.¹⁴ The Court found that the military governor was acting on behalf of the de facto government of Venezuela and held that his actions were unreviewable by a United

ance of the Costa Rican government's directives prohibiting external debt repayment. *Id.* at 874-75. Both Costa Rica and the United States are signatories of the IMF Agreement. *Id.* at 897. Moving for reargument of plaintiff's motion for summary judgment, which had been granted by the court, the Costa Rican bank defendant invoked article VIII, § 2(b), and contended that the Costa Rican directives were exchange control regulations that were imposed consistently with the Bretton Woods Agreement. *Id.* at 897. The Costa Rican bank alleged that the loan agreements were thus invalid under article VIII, § 2(b), as "exchange contracts" contrary to the Costa Rican directives. *Id.* The *Libra* court construed "exchange contract" narrowly to include only contracts "for the exchange of one currency against another or one means of payment against another." *Id.* (quoting 2 J. GOLD, *THE FUND AGREEMENT IN THE COURTS* 425 (1982)). Accordingly, the *Libra* court found that the international loan agreement was not an "exchange contract" under the Bretton Woods Agreement. 570 F. Supp. at 900. The *Libra* court further noted that even if the loan agreements were "exchange contracts," no authority supported the proposition that a currency regulation, such as the Costa Rican directives, adopted *after* the formation of the exchange contract (the loan agreements) could render the exchange contract invalid. *Id.* Finally, the court noted that no evidence demonstrated that the Costa Rican directives were consistent with the IMF Articles of Agreement. *Id.* at 901. For a discussion of the *Libra* case with respect to its act of state analysis, see *infra* note 126.

Considerable disagreement exists as to whether article VIII, § 2(b), of the Bretton Woods Agreement includes international loan transactions within the term "exchange contract". See Ebenroth & Teitz, *supra* note 6, at 248. United States courts typically have adopted the narrow construction of exchange contracts. *Id.* Several scholars and some European courts, however, have adopted a broad construction that would include international loan agreements or any other contracts affecting monetary elements. See *id.*; Williams, *Extraterritorial Enforcement of Exchange Control Regulations under the International Monetary Fund Agreement*, 15 VA. J. INT'L L. 319 (1975). Thus, article VIII, § 2(b), of the Bretton Woods Agreement potentially could emerge as the controlling legal principle in United States courts for determining the validity of international loan transactions.

13. 168 U.S. 250 (1897).

14. *Id.* at 251. In *Underhill*, the plaintiff, an American citizen, was living in Venezuela where he had constructed a waterworks and carried on a machinery repair business. *Id.* When the revolutionary government of Hernandez rose to power, Underhill made several requests for a passport to leave Venezuela. *Id.* The Hernandez government, which was recognized by the United States as the legitimate government of Venezuela, repeatedly denied Underhill's request before finally granting him a passport. *Id.* Subsequently, Underhill brought an action against Hernandez in the Second Circuit for damages that arose as a result of his confinement in Venezuela. *Id.* The trial court held for the defendant on the grounds that he was acting on behalf of the de facto government of Venezuela. *Id.* at 251-52.

States court.¹⁵ The Court, in reaching this decision, stated:

Every sovereign State is bound to respect the independence of every other sovereign State, and the courts of one country will not sit in judgment on the acts of the government of another done within its own territory. Redress of grievances by reason of such acts must be obtained through the means open to be availed of by sovereign powers as between themselves.¹⁶

The modern statement of the act of state doctrine was expressed in *Banco Nacional de Cuba v. Sabbatino*,¹⁷ in which the Supreme Court held:

[T]he Judicial Branch will not examine the validity of a taking of property within its own territory by a foreign sovereign government, extant and recognized by this country at the time of the suit, in the absence of treaty or other unambiguous agreement regarding controlling legal principles, even if the complaint alleges that the taking violates customary international law.¹⁸

15. *Id.* at 254.

16. *Id.* at 252.

17. 376 U.S. 398 (1964). In *Sabbatino*, an American commodity broker, Farr, Whitlock & Co. (Farr, Whitlock), contracted to purchase sugar from Compania Azucarera Vertientes-Camaguey de Cuba (C.A.V.), a Cuban corporation largely owned by United States residents. *Id.* at 401. Thereafter, C.A.V. was nationalized by Fidel Castro's regime. *Id.* Following the nationalization, Farr, Whitlock was required to enter into new contracts with an instrumentality of the Cuban government in order to receive delivery of the sugar expropriated from C.A.V. *Id.* at 403-05. The sugar was then delivered to Farr, Whitlock's customer in Morocco. *Id.* at 405.

The Cuban instrumentality assigned its interest in the Farr, Whitlock contract to Banco Nacional de Cuba (Banco Nacional). *Id.* When Banco Nacional sought payment for the sugar through its agent in New York, Farr, Whitlock refused to pay even though it had received payment from its customer. *Id.* at 405-06. Farr, Whitlock was acting at the request of C.A.V., which claimed it was rightfully entitled to payment for the expropriated sugar and which agreed to indemnify Farr, Whitlock for any loss. *Id.* at 405. Sabbatino was then appointed temporary receiver of the proceeds paid to Farr, Whitlock for the sugar. *Id.* at 406.

Banco Nacional brought suit in the United States District Court for the Southern District of New York to recover those proceeds in an action for conversion of the bills of lading. *Id.* The district court held that the Cuban expropriation violated international law and was ineffective to pass title of the sugar from C.A.V. to the Cuban instrumentality. *Id.* The district court found that the act of state defense was not available to Banco Nacional since the Cuban act violated international law. *Id.* at 406-07. The Second Circuit affirmed, relying on two State Department letters indicating the Executive Branch's willingness to judicially test the Cuban expropriation decrees. *Id.* at 407. For a discussion of the lower court opinions in *Sabbatino*, see Lillich, *A Pyrrhic Victory at Foley Square: The Second Circuit and Sabbatino*, 8 VILL. L. REV. 155 (1962).

18. 376 U.S. at 428.

Although the *Underhill* and *Sabbatino* formulations of the act of state doctrine may seem to suggest that a court should decline jurisdiction and exercise judicial restraint in appropriate circumstances, the doctrine actually functions as a special choice of law rule.¹⁹ The traditional rule for determining the appropriate law in a case involving an act of a foreign sovereign is to apply the law of the state where the act took place.²⁰ An exception to this rule arises where that law violates the public policy of the forum.²¹ Where a foreign state acts within its own territory, the act of state doctrine effectively precludes this public policy exception to the traditional choice of law rule.²² In appropriate circumstances, the doctrine will also override contractual agreements specifying the choice of law.²³ In *Ricaud v. American Metal Co.*,²⁴ the Supreme Court explained

19. See Crockett, *Choice of Law Aspects of the Foreign Sovereign Immunities Act of 1976*, 14 LAW & POL'Y INT'L BUS. 1041, 1053-54 (1983). The *Underhill* formulation of the doctrine, including the statement that a court will not "sit in judgment on the acts of a government of another," is misleading since it suggests that a court shall decline jurisdiction. See *id.* at 1053 (citing *Underhill*, 168 U.S. at 252). See also RESTATEMENT OF FOREIGN RELATIONS LAW OF THE UNITED STATES (REVISED) § 469 reporter's note 1 (Tent. Draft No. 6, 1985) [hereinafter cited as RESTATEMENT (REVISED)]. This note provides:

In most cases, the act of state doctrine may be seen as a special rule of conflict of laws. The normal rule of choice of law in most act of state cases would point to application of the law of the state where the act took place; that rule may be disregarded in certain instances where the law thus chosen would violate the strong public policy of the forum, e.g., a policy against expropriation without compensation. . . . The act of state doctrine precludes giving effect to that public policy to deny effect to the foreign law.

Id. (citing RESTATEMENT (SECOND) OF CONFLICT OF LAWS § 90 (1971)). See also Henkin, *Act of State Today: Recollections in Tranquility*, 6 COLUM. J. TRANSNAT'L L. 175, 178 (1967) ("[a]ct of state is a special rule modifying the ordinary rules of conflict of laws").

20. See RESTATEMENT (REVISED), *supra* note 19, § 469 reporters note 1.

21. See *id.* See also A. KUHN, COMPARATIVE COMMENTARIES ON PRIVATE INTERNATIONAL LAW OR CONFLICT OF LAWS 33-44 (1981) (describing historical basis for public policy as a general limitation upon domestic recognition of foreign law).

22. See RESTATEMENT (REVISED), *supra* note 19, § 469 reporter's note 1.

23. See RESTATEMENT (REVISED), *supra* note 19, § 469 comment e. Sovereign governments or private parties involved in an international agreement generally may specify in the agreement a choice of law to govern their rights and liabilities. See 2 P. WOOD, *supra* note 12, §§ 1.01-.04 (1986). For example, in a loan transaction, the parties may specify in the loan contracts that the law of the lender's country will govern the contract so as to insulate the loan agreement from "political interference by legal changes effected in the borrower's country." *Id.* § 1.03[4]. However, as is stated in the *Restatement of Foreign Relations Law*, the act of state doctrine may render any contractually specified choice of law meaningless so that the act of state becomes the applicable law to govern the transaction. RESTATEMENT (REVISED), *supra* note 19, § 469 comment e. This comment to the *Restatement* provides that the act of state doctrine cannot be "waived" by the foreign state, and that "indications of consent to adjudication by the courts of another state are highly relevant, though not conclusive." *Id.*

24. 246 U.S. 304 (1918). In *Ricaud*, the plaintiff, a United States citizen,

the effect of characterizing the act of state doctrine as a choice of law rule. The Court observed that the act of state doctrine does not deprive a court of jurisdiction over a case.²⁵ Rather, where the doctrine is applicable, a court must exercise jurisdiction, construe the foreign sovereign's act as a valid exercise of its authority, and accept the act as the rule of decision in the case.²⁶

While there is general agreement that the act of state doctrine functions as a "super choice-of-law" principle,²⁷ the Supreme Court has not been clear or consistent in explicating the doctrine's underlying rationales. Over the years, the Court has enunciated a variety of justifications for the doctrine.²⁸ In *Underhill*, the Court's opinion suggested that the inherent nature of sovereign authority grants a foreign sovereign state immunity from domestic judicial review of acts done within the sovereign's own territory.²⁹

purchased lead bullion from a Mexican mining company. *Id.* at 306. The lead bullion was confiscated by a revolutionary Mexican general during the Mexican Revolution. *Id.* The Supreme Court ruled that the validity of the confiscation could not be examined because it was a Mexican act of state within Mexican borders. *Id.* at 310.

25. *Id.* at 309.

26. *Id.* The Court stated:

[The act of state doctrine] does not deprive the courts of jurisdiction once acquired over a case. It requires only that, when it is made to appear that the foreign government has acted in a given way on the subject-matter of the litigation, the details of such action or the merit of the result cannot be questioned but must be accepted by our courts as a rule for their decision. To accept a ruling authority and to decide accordingly is not a surrender or abandonment of jurisdiction but is an exercise of it.

Id. See also Halberstam, *Sabbatino Resurrected: The Act of State Doctrine in the Revised Restatement of U.S. Foreign Relations Law*, 79 AM. J. INT'L L. 68, 74-76 (1985); Crockett, *supra* note 19, at 1053-54; Henkin, *supra* note 19, at 178.

27. See Dellapenna, *Suing Foreign Governments and Their Corporations: Choice of Law* (pt. 6), 87 COM. L.J. 129, 130 n.15 (1982) (in most recent Supreme Court decision on act of state doctrine, seven Justices endorsed view that doctrine requires court to use foreign law as rule of decision) (citing *Alfred Dunhill, Inc. v. Cuba*, 425 U.S. 682, 705 n.18, 726-28 (1976)).

28. See, e.g., Conant, *The Act of State Doctrine and Its Exceptions: An Introduction*, 12 VAND. J. TRANSNAT'L L. 259 (1979) (describing and criticizing variety of justifications posited by Supreme Court and lower courts invoking act of state doctrine). See also RESTATEMENT (REVISED), *supra* note 19, § 469 comment a.

29. 168 U.S. at 252. In its brief opinion, the *Underhill* Court focused mainly on the issue of whether Hernandez, as military chief of the revolutionary government of Venezuela, was acting under the authority of the revolutionary government of Venezuela, which was recognized by the United States as the government of the country. *Id.* at 253-54. The Court agreed with the finding of the lower court that "the evidence upon the trial indicated that the purpose of the defendant in his treatment of the plaintiff was to coerce the plaintiff to operate his waterworks and his repair works for the benefit of the community and the revolutionary forces." *Id.* at 254 (quoting *Underhill v. Hernandez*, 65 F. 577, 579 (2d Cir. 1895)). The Court's emphasis on absolute sovereign immunity was evidenced by its conclusion that "[t]he immunity of individuals from suits brought in foreign tribunals for acts done within their own states, in the exercise

The opinion of the Court of Appeals for the Second Circuit in *Underhill* revealed a second rationale for the doctrine, which the Supreme Court expressly relied on in later decisions.³⁰ The Second Circuit stated that international comity justifies recognition of the validity of foreign acts of state in appropriate circumstances.³¹ The principle of international comity holds that a domestic court may give effect to a foreign act where such recognition would serve "international duty and convenience" and would not undermine the rights of any citizens within the forum.³² Accordingly, comity operates as an exception to one of the

of governmental authority, whether as civil officers or as military commanders, must necessarily extend to the agents of governments ruling by paramount force as a matter of fact." *Id.* at 252. See also Note, *Rehabilitation and Exoneration of the Act of State Doctrine*, 12 N.Y.U. J. INT'L L. & POL. 599, 604 (1980). This commentator suggests that Chief Justice Fuller's act of state formulation in *Underhill* was an expression of his dissatisfaction with the outcome of two other Supreme Court cases decided in that era which were not in accordance with the notion of absolute sovereign immunity. *Id.* at 604-05. In *Hilton v. Guyot*, the Supreme Court refused to enforce a French judgment entered against an American citizen. 159 U.S. 113, 227-29 (1895). In *The Paquete Habana*, the Court invalidated the seizure of two Spanish fishing vessels by the United States during the Spanish-American War. 175 U.S. 677, 678, 714 (1900). In each of these cases, Chief Justice Fuller dissented, reflecting his broad conviction that "courts should abstain from adjudicating disputes involving acts of foreign states." Note, *supra*, at 605.

30. *Underhill v. Hernandez*, 65 F. 577 (2d Cir. 1895), *aff'd*, 168 U.S. 250 (1897).

31. *Id.* at 579. In *Underhill*, the Second Circuit held that military and civil public agents of foreign governments are immune from suit in the United States. *Id.* at 583. Although the court based its decision on the jurisdictional issue of sovereign immunity, it relied on the theory of international comity as a justification for its decision:

Considerations of comity, and of the highest expediency, require that the conduct of states . . . should not be called in question by the legal tribunals of another jurisdiction. The citizens of a state have an adequate redress for any grievances at its hands by an appeal to . . . the other departments of their own government. . . . [I]t would imperil the amicable relations between governments, and vex the peace of nations, to permit the sovereign acts or political transactions of states to be subjected to the examination of the legal tribunals of other states.

Id. at 579. See generally Comment, *The Act of State Doctrine and Foreign Sovereign Defaults on United States Bank Loans: A New Focus for a Muddled Doctrine*, 133 U. PA. L. REV. 469, 471-74 (1985) (describing policy justifications for act of state doctrine suggested by the *Underhill* opinions).

32. See *Hilton v. Guyot*, 159 U.S. 113, 163-64 (1895).

In *Hilton*, the Supreme Court made the following concise statement of the principle of international comity:

No law has any effect, of its own force, beyond the limits of the sovereignty from which its authority is derived. The extent to which the law of one nation, as put in force within its territory, whether by executive order, by legislative act, or by judicial decree, shall be allowed to operate within the dominion of another nation, depends upon . . . "the comity of nations."

...

"Comity," in the legal sense, is neither a matter of absolute obliga-

fundamental maxims of private international law—that no law of a sovereign government is effective outside the sovereign's own territory.³³ In American jurisprudence, comity is employed to modify this territorial rule since its rigid application would be detrimental to amicable relations among nations.³⁴

In *Oetjen v. Central Leather Co.*,³⁵ the Supreme Court reaffirmed the principle of international comity as a policy justification for the act of state doctrine as was suggested by the Second Circuit's opinion in *Underhill*.³⁶ In *Oetjen*, the Court refused to question the validity of an expropriation by the Mexican government during the Mexican Revolution of 1913-1914.³⁷ The Court stated that the act of state doctrine rested "upon the highest considerations of international comity and expediency."³⁸ The Court reasoned that to permit the validity of the acts of one sovereign state to be reexamined and perhaps condemned by the

tion, on the one hand, nor of mere courtesy and good will, upon the other. But it is the recognition which one nation allows within its territory to the legislative, executive or judicial acts of another nation, having due regard both to international duty and convenience, and to the rights of its own citizens or of other persons who are under the protection of its laws.

Id.

33. See A. KUHN, *supra* note 21, at 28-33. Professor Kuhn explains that "Private International Law or the Conflict of Laws is that branch of legal science which seeks to determine the application of law when the administration of justice requires a choice between two or more systems of law." *Id.* at 1. International comity, as a doctrinal foundation of private international law in the United States, recognizes that a sovereign may allow recognition of foreign law in cases where "no sovereign right was surrendered nor the rights of native subjects injured." *Id.* at 28-29. See also A. EHRENZWEIG, CONFLICT OF LAWS 161-66 (1962); Yntema, *The Comity Doctrine*, 65 MICH. L. REV. 9 (1966) (historical explanation of international comity).

34. See A. KUHN, *supra* note 21, at 29 (in theory, comity "seemed ideal to modify and temper the rigorous application of territorial law and to accord recognition to foreign law on local territory"); Maier, *Extraterritorial Jurisdiction at a Crossroads: An Intersection Between Public and Private International Law*, 76 AM. J. INT'L L. 280, 281-85 (1982). Maier observes that, in American jurisprudence, the application of comity to recognize foreign law is based on a judicial concern for "the maintenance of amicable external relations with other nation-states." *Id.* at 283.

35. 246 U.S. 297 (1918).

36. *Id.* at 303-04; *Underhill*, 65 F. 577, 579 (2d Cir. 1895), *aff'd*, 168 U.S. 250 (1897).

37. 246 U.S. at 299-300, 303. The case involved a title dispute over animal hides seized from a Mexican national by the de facto Mexican government during the Mexican Revolution of 1913-1914. *Id.* at 299-300. The confiscated hides were sold to an American company which in turn sold them to the defendant. *Id.* at 299. The plaintiff, as assignee of the original owner of the hides, brought an action for replevin in the federal circuit court in New Jersey. *Id.* Based on the act of state doctrine, the Supreme Court affirmed the lower court's refusal to pass judgment on the validity of the Mexican act of confiscation. *Id.* at 303-04.

38. *Id.* at 303-04.

courts of another sovereign would "imperil the amicable relations between governments and vex the peace of nations."³⁹

In *Sabbatino*, the Court shifted its justification for the act of state doctrine.⁴⁰ The Court concluded that the doctrine had "'constitutional' underpinnings" arising "out of the basic relationships between branches of government in a system of separation of powers."⁴¹ The act of state doctrine, the Court noted, represents an acknowledgement by the judicial branch that in some cases adjudication of the acts of a foreign sovereign may impede foreign relations goals sought by the political branches.⁴²

39. *Id.* (quoting *Underhill v. Hernandez*, 65 F. 577 (2d Cir. 1895), *aff'd.*, 168 U.S. 250 (1897)).

40. 376 U.S. at 427-28. For a discussion of *Sabbatino*, see *supra* note 17 and accompanying text.

41. 376 U.S. at 423. The *Sabbatino* Court stated, "We do not believe that this doctrine is compelled either by the inherent nature of sovereign authority . . . or by some principle of international law." *Id.* at 421.

42. *Id.* at 423-27. The Court noted that "[t]he text of the Constitution does not require the act of state doctrine; it does not irrevocably remove from the judiciary the capacity to review the validity of foreign acts of state." *Id.* at 423. The Court expressly narrowed the statement by the *Oetjen* Court that "[t]he conduct of the foreign relations of our government is committed by the Constitution to the Executive and Legislative . . . Departments." *Id.* (quoting *Oetjen*, 246 U.S. at 302) (emphasis added).

The separation of powers rationale relied upon in *Sabbatino* is widely regarded as the modern justification for the act of state doctrine. See, e.g., Ebenroth & Teitz, *supra* note 6, at 227-29. While the early cases involving the act of state doctrine rested on the theories of sovereign immunity and comity, the second sentence of the Court's formulation of the doctrine in *Underhill* suggests that the separation of powers rationale may have been a basis for the doctrine at its inception: "Redress of grievances by reason of such acts must be obtained through the means open to be availed of by sovereign powers as between themselves." 168 U.S. at 252 (emphasis added).

The *Sabbatino* Court's deference to the political branches in matters of foreign policy is akin to the political question doctrine. See RESTATEMENT (REVISED), *supra* note 19, § 469 comment a. The political question doctrine provides that issues political in nature are inappropriate for judicial consideration. J. NOWAK, R. ROTUNDA & J. YOUNG, CONSTITUTIONAL LAW 109-20 (2d ed. 1983). The political question doctrine was summarized in *Baker v. Carr*, in which the Supreme Court stated:

Prominent on the surface of any case held to involve a political question is found a textually demonstrable constitutional commitment of the issue to a coordinate political department; or a lack of judicially discoverable and manageable standards for resolving it; or the impossibility of deciding without an initial policy determination of a kind clearly for nonjudicial discretion; or the impossibility of a court's undertaking independent resolution without expressing lack of the respect due coordinate branches of government; or an unusual need for unquestioning adherence to a political decision already made; or the potentiality of embarrassment from multifarious pronouncements by various departments on one question.

369 U.S. 186, 217 (1962). The *Baker* Court noted that where a court is faced with issues implicating foreign affairs, the issues often fall squarely within the scope of the political question doctrine:

The *Sabbatino* Court enumerated two broad guidelines for determining where separation of powers concerns would arise so as to justify application of the act of state doctrine: (1) where there is no "codification or consensus" regarding a facet of international law,⁴³ and (2) where an important issue of foreign policy is implicated.⁴⁴ In these situations, the Court concluded, the political branches may possess exclusive power.⁴⁵

III. LIMITATIONS AND EXCEPTIONS TO THE ACT OF STATE DOCTRINE

United States courts have articulated numerous limitations and exceptions to the act of state doctrine.⁴⁶ Of these, the territorial limita-

Not only does resolution of such issues [touching on questions of foreign relations] frequently turn on standards that defy judicial application, or involve the exercise of a discretion demonstrably committed to the executive or legislature; but many such questions uniquely demand single-voiced statement of the Government's views.

Id. at 211 (footnotes omitted). See also J. NOWAK, R. ROTUNDA, & J. YOUNG, *supra*, at 198. Thus, in many cases the political question doctrine will render an issue implicating foreign affairs nonjusticiable. In contrast, under the act of state doctrine, a court that clearly has power to decide a case must consider the act of a foreign sovereign as the rule for its decision where failure to do so may interfere with the conduct of foreign affairs by the political branches. See Note, *Adjudicating Acts of State in Suits Against Foreign Sovereigns: A Political Question Analysis*, 51 FORDHAM L. REV. 722, 742-43 (1983). However, as the Court of Appeals for the Ninth Circuit has noted, the act of state doctrine and the political question doctrine are analogous insofar as they both require courts to recognize that the executive and legislative branches are better equipped to handle politically sensitive issues than the judicial branch. *Northrop Corp. v. McDonnell Douglas Corp.*, 705 F.2d 1030, 1046 (9th Cir.), *cert. denied*, 464 U.S. 849 (1983).

43. 376 U.S. at 428. The Court stated:

It should be apparent that the greater the degree of codification or consensus concerning a particular area of international law, the more appropriate it is for the judiciary to render decisions regarding it, since the courts can then focus on the application of an agreed principle to circumstances of fact rather than on the sensitive task of establishing a principle not inconsistent with the national interest or with international justice.

Id.

44. *Id.* The Court observed: "It is also evident that some aspects of international law touch much more sharply on national nerves than do others; the less important the implications of an issue are for our foreign relations, the weaker the justification for exclusivity in the political branches." *Id.* Thus, issues with little impact on United States foreign policy may not require exclusive consideration by the political branches. *Id.*

45. See *id.*

46. See Recent Development, *International Law—Act of State Doctrine—First National City Bank v. Banco Nacional de Cuba*, 49 WASH. L. REV. 213 (1973). This commentator observed:

Support exists in varying degrees for assertions that the doctrine should not apply when (1) the foreign state is at war with the United States, (2) the foreign state is not recognized by the United States, (3) the suit is brought to enforce a foreign state's penal or revenue laws, (4) the act was not performed within the territory of the foreign

state, (5) the foreign government is not in existence at the time of suit, (6) the act was not fully executed, (7) the act is illegal under the law of the foreign state, (8) a treaty or other unambiguous agreement covers the controversy or (9) there is a "clear" violation of international law.

Id. at 223-24 (footnotes omitted).

There also are exceptions for counterclaims, commercial activities, executive suggestions, and acts of government functionaries done without sovereign authority. *See* Comment, *supra* note 32, at 472 n.16.

The commercial activity exception to the act of state doctrine provides that private commercial acts of a foreign sovereign state do not fall within the act of state doctrine. *See* *Alfred Dunhill, Inc. v. Republic of Cuba*, 425 U.S. 682, 697-98 (1976) (plurality opinion). In *Dunhill*, four members of the Supreme Court recognized the validity of the exception. *Id.* at 684. The case involved five major Cuban cigar exporting companies that were nationalized by Castro's government. *Id.* at 685. Cuba refused to repay the former owners of the companies, most of whom had fled to the United States, for amounts United States importers had mistakenly paid to the agents of the Cuban government who had taken over management of the nationalized companies (the "interventors"). *Id.* at 685-87. The interventors claimed that their repudiation of the obligation to the former owners was an act of state which must be recognized by a United States court. *Id.* at 687. The *Dunhill* plurality held that the interventors' refusal to return the money was an exercise of commercial authority not within the act of state doctrine. *Id.* at 695-706.

The *Allied II* court decided not to apply the act of state doctrine; therefore it did not address the commercial activity exception. *See* *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 757 F.2d 516, 518 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985). However, the applicability of the exception was considered and rejected in two subsequent cases involving the effect of foreign governmental currency controls on private obligations. *See* *Callejo v. Bancomer, S.A.*, 764 F.2d 1101, 1114-16 (5th Cir. 1985); *Braka v. Bancomer, S.N.C.*, 762 F.2d 222, 225 (2d Cir. 1985). *Callejo* involved Mexican exchange control regulations that compelled a Mexican bank to pay substantially less than the face value of certificates of deposit owned by United States citizens. 764 F.2d at 1106. The certificate holders alleged that the act of state doctrine was not applicable since the transaction in the case was a commercial activity. *Id.* at 1114-16. The court noted first that the validity of the commercial activity exception was uncertain, and further stated that were it a valid exception, it would not apply to the Mexican exchange control regulations. *Id.* at 1114-16 & 1115 n.17. The court stated that "[t]he power to issue exchange control regulations is paradigmatically sovereign in nature; it is not of a type that a private person can exercise. Unlike *Dunhill*, where Cuba repudiated a single debt, here Mexico promulgated comprehensive, national decrees in response to a national monetary crisis." *Id.* at 1116.

In addition, there exists a legislative exception to the act of state doctrine known as the "Hickenlooper Amendment." *See* 22 U.S.C. § 2370(e)(2) (1982). Displeased with the *Sabbatino* decision, Congress sought to modify the result when it passed the Hickenlooper Amendment to the Foreign Assistance Act of 1964. *See* Dellapenna, *Suing Foreign Governments and Their Corporations: Choice of Law* (pt. 5), 87 Com. L.J. 8, 11 (1982). The Hickenlooper Amendment states:

(2) Notwithstanding any other provision of law, no court in the United States shall decline on the ground of the federal act of state doctrine to make a determination on the merits giving effect to the principles of international law in a case in which a claim of title or other rights to property is asserted by any party including a foreign state (or a party claiming through such state) based upon (or traced through) a confiscation or other taking after January 1, 1959, by an act of that state in violation of the principles of international law, including the princi-

tion⁴⁷ and the *Bernstein* exception⁴⁸ are especially pertinent to the *Allied*

ples of compensation and the other standards set out in this subsection: *Provided*, That this subparagraph shall not be applicable (1) in any case in which an act of a foreign state is not contrary to international law or with respect to a claim of title or other right to property acquired pursuant to an irrevocable letter of credit of not more than 180 days duration issued in good faith prior to the time of the confiscation or other taking, or (2) in any case with respect to which the President determines that application of the act of state doctrine is required in that particular case by the foreign policy interests of the United States and a suggestion to this effect is filed on his behalf in that case with the court.

22 U.S.C. § 2370(e)(2) (1982). The constitutionality of this amendment was upheld in *Banco Nacional de Cuba v. Farr*, 243 F. Supp. 957, 971-77 (S.D.N.Y. 1965), *aff'd*, 383 F.2d 166 (2d Cir. 1967), *cert. denied*, 390 U.S. 956 (1968). Notwithstanding the Hickenlooper Amendment, the *Sabbatino* case continues to provide the leading authority on the act of state doctrine. *See, e.g.*, *Industrial Inv. Dev. Corp. v. Mitsui & Co.*, 594 F.2d 48, 51 n.7 (5th Cir. 1979), *cert. denied*, 445 U.S. 903 (1980). Application of the amendment has been judicially limited to cases in which property is confiscated by a foreign sovereign while within the sovereign's borders, but which is subsequently brought into the United States. *See, e.g.*, *Banco Nacional de Cuba v. First Nat'l City Bank*, 431 F.2d 394 (2d Cir. 1970), *rev'd on other grounds*, 406 U.S. 759 (1972); *French v. Banco Nacional de Cuba*, 23 N.Y.2d 46, 272 N.E.2d 704, 295 N.Y.S.2d 443 (1968). Additionally, the Hickenlooper Amendment has not been applied to confiscations of property owned by a national of the foreign sovereign. *See F. Palicio y Compania, S.A. v. Brush*, 256 F. Supp. 481, 487 (S.D.N.Y. 1966), *aff'd per curiam*, 375 F.2d 1011 (2d Cir.), *cert. denied*, 389 U.S. 830 (1967). For a further discussion of the Hickenlooper Amendment, see Henkin, *supra* note 19, at 178-85; Comment, *The Act of State Doctrine: A History of Judicial Limitations and Exceptions*, 18 HARV. INT'L L.J. 677, 679 n.4 (1977).

The complexity of the exceptions and limitations of the act of state doctrine is evidenced by the Supreme Court's most recent decision on that subject. *See Alfred Dunhill, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976). For an analysis of *Dunhill* and its impact upon the current status of the act of state doctrine, see Dellapenna, *Suing Foreign Governments and Their Corporations: Choice of Law* (pts. 3-5), 86 Com. L.J. 438 (1981), 86 Com. L.J. 486 (1981), 87 Com. L.J. 8 (1982). Professor Dellapenna notes that in the one plurality, two concurring and one dissenting opinions in *Dunhill*, the Court articulated the following seven distinct theories of the act of state doctrine, none of which commanded the support of more than four Justices: (1) the doctrine was inapplicable because the Government was acting in a commercial capacity; (2) the doctrine functioned exactly like the political question doctrine; (3) the doctrine was applicable, without exception, to any situation involving an act of state; (4) the doctrine was not applicable to counterclaims against a foreign sovereign government; (5) the doctrine was inapplicable when the executive branch has indicated that it would not be embarrassed by such an inquiry; (6) the doctrine was inapplicable because the acts in question were not sovereign acts; and (7) the doctrine was inapplicable because the acts were extraterritorial. Dellapenna (pt. 3), *supra*, at 444-45.

47. Since its inception, the act of state doctrine has been limited to acts of a foreign sovereign "*done within its own territory*." *See Underhill*, 168 U.S. at 252 (emphasis added).

48. The *Bernstein* exception applies where the Executive has suggested that the act of state doctrine should not be applied by a court. *See Bernstein v. Van Heyghen Freres Societe Anonyme*, 163 F.2d 246, 251 (2d Cir.), *cert. denied*, 332 U.S. 772 (1947). For a discussion of the *Bernstein* exception, see *infra* notes 101-20 and accompanying text.

case.

A. *The Territorial Limitation*

Since *Underhill*, courts have limited the act of state doctrine to acts of a foreign sovereign done "within its own territory."⁴⁹ In so limiting the doctrine, United States courts respect the expectations of foreign governments in territorial sovereignty and further recognize the practical inability of a court to review and "invalidate" a sovereign act affecting property wholly within the sovereign's dominion.⁵⁰ A foreign government should expect, however, that its extraterritorial acts will be subject to judicial review and there exists a diminished risk that such review will affront the foreign government.⁵¹

The territorial limitation is straightforward in its application to tangible property with a known location;⁵² however, when intangible property such as a debt is involved, its application is less clear.⁵³ Courts are faced with the difficult problem of siting the intangible property to determine whether the foreign sovereign's act affected property within its own territory.

The earliest act of state cases involving intangible property arose in the Second Circuit and involved attempted seizures of intangible property by foreign sovereign states.⁵⁴ The Second Circuit's determination

49. *Underhill*, 168 U.S. at 252. Since *Underhill*, the territorial limitation to the act of state doctrine has been consistently recognized. See Zaitzeff & Kunz, *The Act of State Doctrine and the Allied Bank Case*, 40 BUS. LAW. 449, 451 (1985).

50. See, e.g., *Tabacalera Severiano Jorge, S.A. v. Standard Cigar Co.*, 392 F.2d 706, 715 (5th Cir.), cert. denied, 393 U.S. 924 (1968). The court observed that act of state decisions plainly "took into consideration the realization that in most situations there was nothing the United States courts could do . . . in any event." *Id.* See also Zaitzeff & Kunz, *supra* note 49, at 451-52.

51. *Tabacalera Severiano Jorge, S.A. v. Standard Cigar Co.*, 392 F.2d 706, 715 (5th Cir.), cert. denied, 393 U.S. 924 (1968). The court stated:

The underlying thought expressed in all of the cases touching on the Act of State Doctrine is a common-sense one. It is that when a foreign government performs an act of state which is an accomplished fact, that is when it has the parties and the *res* before it and acts in such a manner as to change the relationship between the parties touching the *res*, it would be an affront to such foreign government for courts of the United States to hold that such act was a nullity.

Id. See also Zaitzeff & Kunz, *supra* note 49, at 451-52.

52. See, e.g., *Oetjen*, 246 U.S. 297 (1918) (Mexican seizure of animal hides was act of state within Mexican borders so doctrine was applicable). See also Conant, *supra* note 28, at 259-60. Professor Conant noted that the act of state doctrine was developed to apply to expropriations, nationalizations, or confiscations of tangible property by foreign sovereign governments. *Id.*

53. See *Tabacalera Severiano Jorge, S.A. v. Standard Cigar Co.*, 392 F.2d 706, 714 (5th Cir.), cert. denied, 393 U.S. 924 (1968). The *Tabacalera* court observed, "The situs of an intangible property is about as intangible a concept as is known to the law." *Id.*

54. See *Menendez v. Saks & Co.*, 485 F.2d 1355 (2d Cir. 1973), *rev'd on other grounds sub nom.* *Alfred Dunhill, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976);

of the situs of intangible property in these early cases focused on either the sovereign's power to enforce its purported seizure of the debt (enforcement test)⁵⁵ or on the location of the debtor.⁵⁶

Republic of Iraq v. First Nat'l City Bank, 353 F.2d 47 (2d Cir. 1965), *cert. denied*, 382 U.S. 1027 (1966). See also *Vishipco Line v. Chase Manhattan Bank*, 660 F.2d 854 (2d Cir. 1981), *cert. denied*, 459 U.S. 976 (1982); *United Bank Ltd. v. Cosmic Int'l, Inc.*, 542 F.2d 868 (2d Cir. 1976); Comment, *supra* note 46, at 683-88.

55. See, e.g., *Republic of Iraq v. First Nat'l City Bank*, 353 F.2d 47, 51 (2d Cir. 1965), *cert. denied*, 382 U.S. 1027 (1966). The government of Iraq issued an ordinance authorizing seizure of a bank account and stock held in a custodial account in New York by King Faisal II, who was killed during the Iraqi revolution of 1958. *Id.* at 49. Pursuant to the ordinance, the government of Iraq sued the administrator of Faisal's New York assets for recovery of the assets. *Id.* at 49-50. Iraq tried to invoke the act of state doctrine with respect to its ordinance by claiming that the property affected was located in Iraq because King Faisal II resided and was physically present in Iraq. *Id.* at 51. The Court rejected this contention, reasoning that the property would be deemed to be located in Iraq only if the defendant bank could be compelled by an Iraqi court to deliver the property of King Faisal that it held in the custodial account to the Iraqi government. *Id.* See also *Menendez v. Saks & Co.*, 485 F.2d 1355, 1364 (2d Cir. 1973) ("For purposes of the act of state doctrine, a debt is not 'located' within a foreign state unless that state has the power to enforce or collect it."), *rev'd on other grounds sub nom.* *Alfred Dunhill, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976); Comment, *supra* note 46, at 684-86. This commentator observes that while dicta in the *Menendez* case suggests that if the foreign sovereign has jurisdiction over the defendant, the "enforcement test" is met, the Second Circuit subsequently has held that jurisdiction over the defendant is not determinative. *Id.* at 685 (citing *United Bank Ltd. v. Cosmic Int'l*, 542 F.2d 868 (2d Cir. 1976)). This commentator adds that "[i]t is probable that the original reference to jurisdiction in the *Menendez* dictum meant only that the power to enforce payment of a debt generally depends on jurisdiction over the person of the debtor; i.e., jurisdiction is a necessary condition for enforcement, but alone not a sufficient one." *Id.* at 685 n.42 (citing *Menendez v. Saks & Co.*, 485 F.2d 1355, 1365 (2d Cir. 1973), *rev'd on other grounds sub nom.* *Alfred Dunhill, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976)). Accord, *Rupali Bank v. Provident Nat'l Bank*, 403 F. Supp. 1285 (E.D. Pa. 1975).

56. See, e.g., *United Bank Ltd. v. Cosmic Int'l, Inc.*, 542 F.2d 868, 874 (2d Cir. 1976). This case involved a United States Company (Cosmic) that imported jute products from East Pakistan. *Id.* at 870 n.2. Cosmic owed money to certain Pakistani jute mills for products it received in 1971. *Id.* Before Cosmic made any payment, East Pakistan declared its independence from Pakistan and became Bangladesh. *Id.* at 870. The Bangladesh government nationalized the jute mills and the nationalized companies (Bangladesh plaintiffs) subsequently claimed the right of payment to the Cosmic debt. *Id.* at 871. The Bangladesh plaintiffs argued that the nationalization of the jute mills was an act of state that required the court to give effect to their claims. *Id.* The court decided that it would give effect to the Bangladesh plaintiffs' claims only if the debt owed by Cosmic was located in Bangladesh. *Id.* at 872. The court sited the debt in the United States because that was where the debtor, Cosmic, was found. *Id.* at 874. The court noted that this approach was consistent with a longstanding rule "embedded in American jurisprudence" established in *Harris v. Balk*. *Id.* (citing *Harris v. Balk*, 198 U.S. 215 (1905)). The *Harris* Court held that jurisdiction could be obtained over a defendant domiciled in another state by attachment of the defendant's debt in the forum state. 198 U.S. at 221-23. In reaching this conclusion, the Court stated that the obligation to pay a debt "clings to [the debtor] and accompanies him wherever he goes." *Id.* at 222.

The Court of Appeals for the Fifth Circuit developed a test akin to the Second Circuit's enforcement test in *Tabacalera Severiano Jorge, S.A. v. Standard Cigar Co.*⁵⁷ The test formulated in *Tabacalera*, the *fait accompli* test,⁵⁸ focused solely on whether the foreign sovereign had the power to enforce the purported seizure. The *Tabacalera* case involved a debt owed to a Cuban tobacco company by a United States importer.⁵⁹ The debt was incurred prior to the tobacco company's nationalization by Fidel Castro's regime.⁶⁰ Severiano Jorge, the sole shareholder and assignee of the Cuban company, fled to Florida and subsequently brought suit to collect the debt owed by the importer.⁶¹ The United States importer defended against the claim on act of state grounds arguing that the government of Cuba, by nationalizing the tobacco company, had acquired a right to the debt owed by the United States importer.⁶² In determining the situs of the debt for act of state purposes, the *Tabacalera* court considered whether the Cuban government could have effectively acquired the debt.⁶³ The court concluded that "Cuba was not physically in a position to perform a *fait accompli*" with respect to expropriating the debt because the expropriation could not "come to complete fruition within the dominion of the Cuban government."⁶⁴ The Fifth Circuit, therefore, held that the act of state doctrine was not applicable.⁶⁵

57. 392 F.2d 706 (5th Cir.), *cert. denied*, 393 U.S. 924 (1968).

58. *See* 392 F.2d at 715-16. *See also* *Maltina Corp. v. Cawy Bottling Co.*, 462 F.2d 1021 (5th Cir.) (applying the *fait accompli* test), *cert. denied*, 409 U.S. 1060 (1972).

59. 392 F.2d at 707.

60. *Id.*

61. *Id.* at 708-11. The suit was brought by Tabacalera Severiano Jorge, S.A., the corporation. *Id.* at 711. Before the pleadings were completed, the vice-president of the corporation executed a valid assignment of the corporation's "interest, claim and demand" in the debt to Severiano Jorge, the sole shareholder of the corporation, who had fled to Florida. *Id.*

62. *See id.* at 713-14.

63. *Id.* at 715.

64. *Id.* at 715-16.

65. *Id.* The court reasoned:

In the case before us, it cannot be doubted that whatever may be the ordinary concept of the situs of a debt, the government of Cuba was not physically in a position to perform a *fait accompli* in the nature of the acquisition by the Cuban government . . . of the money owed to Tabacalera by Standard Cigar Company. It was simply not within the power of Cuba to accomplish this result. To this extent, we think it clear that whatever efforts were made by the Cuban government dealing with Tabacalera, these acts are to be recognized under the Act of State Doctrine only insofar as they were able to come to complete fruition within the dominion of the Cuban government.

Id.

The *Tabacalera* or *fait accompli* test was designed by the Fifth Circuit in accordance with the rationale for the territorial limitation to the act of state doctrine. *See id.* at 715. The Fifth Circuit reasoned that, as a practical matter, a court is limited in its ability to nullify sovereign acts done within the sovereign's own territory. *Id.*

More recently, the Second Circuit confronted the problem of applying the act of state doctrine to an intangible debt in *Garcia v. Chase Manhattan Bank*.⁶⁶ In *Garcia*, the court did not delineate a situs test per se, but instead sited the debt by examining the facts and circumstances surrounding the debt, including the terms of the contract at issue.⁶⁷ In *Garcia*, a Cuban citizen, Garcia, purchased a certificate of deposit at the Cuban branch of Chase Manhattan Bank (Chase); by its terms the certificate was payable at any Chase branch worldwide.⁶⁸ Castro nationalized the Cuban branch of Chase, and pursuant to the order of a Cuban ministry, the Cuban branch paid the value of Garcia's certificate to the Cuban government.⁶⁹ Garcia sued Chase in a United States court to recover the money due on the certificate.⁷⁰ In defense, Chase argued that the Cuban expropriation of the funds was an act of state that must be recognized by a United States court.⁷¹ In determining the situs of the debt due on the certificate, the court looked at the intent of the parties when the contract was formed and found that the purpose of the agreement was to insure that Chase would be responsible for the payment or the certificate in any event.⁷² The court also evaluated the terms of the contract, which specified: (1) payment at any Chase branch worldwide, and (2) a guarantee of the certificate of deposit by Chase's New York office.⁷³ Based on these circumstances, the court held that the act of state doctrine was inapplicable.⁷⁴

66. 735 F.2d 645 (2d Cir. 1984). The case was brought before Circuit Judges Meskill, Cardamone, and Kearse. *Id.* at 646.

67. *Id.* at 650-51. See also *Libra Bank Ltd. v. Banco Nacional de Costa Rica, S.A.*, 570 F. Supp. 870, 881-82 (S.D.N.Y. 1983); *Weston Banking Corp. v. Türkiye Garanti Bankası*, 57 N.Y.2d 315, 442 N.E.2d 1195, 456 N.Y.S.2d 684 (1982) (conducting similar factual inquiries).

68. 735 F.2d at 646.

69. *Id.* at 647.

70. *Id.* at 647-48.

71. *Id.* at 650. The *Garcia* court determined that Chase's argument that the appropriation of funds fell within the act of state doctrine was correct if the situs of its debt was Cuba. *Id.* The court questioned, however, whether Cuba actually had seized the debt or whether it seized "merely a payment of a sum equal to it." *Id.*

72. *Id.* at 650-51. Although the *Garcia* court discussed the *Tabacalera* or *fait accompli* test, the court did not perform such an analysis. *Id.* at 650 n.5. For a discussion of the *fait accompli* test, see *supra* notes 57-65 and accompanying text.

73. 735 F.2d at 646, 650-51.

74. *Id.* at 651. In finding the doctrine inapplicable, the court commented: We are not challenging the validity of the Cuban government's actions here and Cuba has shown no interest in the outcome of this case. We are simply resolving a private dispute between an American bank and one of its depositors. The result we reach will have no international repercussions. Chase cannot use the act of state doctrine as a defense because the doctrine is not implicated.

Id.

Judge Kearse wrote a dissenting opinion in *Garcia* criticizing the court's failure to recognize that the debts were collectible in Cuba. *Id.* (Kearse, J., dissent-)

Two recent cases in the Second and Fifth Circuits, arising out of the Mexican economic crisis, further demonstrate the lack of accord as to which situs test applies to intangible property.⁷⁵ In 1982, the Mexican economy suffered from the sharp fall in oil prices which eroded a source of foreign exchange that Mexico needed to repay its enormous foreign debt.⁷⁶ In an effort to stabilize Mexico's economy, the Mexican Ministry of the Treasury and Public Credit issued several decrees mandating that all domestic obligations for payments in foreign currency, including dollar deposits made and payable in Mexico, be performed by delivering pesos at a "special exchange rate" for foreign currency obligations.⁷⁷ Holders of dollar-denominated certificates of deposit in Mexican banks received substantially less than the free market rate when their certificates matured, and as a result, several lawsuits arose in United States courts.⁷⁸

ing). Judge Kearsé noted that the plaintiffs had agreed to payment at any Chase branch worldwide, including Cuba. *Id.* at 652 (Kearsé, J., dissenting). Judge Kearsé invoked the "enforcement test" of locating an intangible property and reasoned that "[t]he applicability of the act of state doctrine to the present case depends on the power of the Cuban government to enforce or collect these debts within Cuba." *Id.* at 651 (Kearsé, J., dissenting) (citation omitted). Since the debt was collected by the Cuban government pursuant to a valid decree at a place where the plaintiff could have collected it, Judge Kearsé reasoned that the debt was extinguished. *Id.* at 652 (Kearsé, J., dissenting). *Cf. Perez v. Chase Manhattan Bank*, 61 N.Y.2d 460, 463 N.E.2d 5, 474 N.Y.S.2d 689, *cert. denied*, 105 S. Ct. 366 (1984). The *Perez* case involved virtually the same facts as *Garcia*, but the New York Court of Appeals held the act of state doctrine applicable based on reasoning similar to Judge Kearsé's dissenting opinion in *Garcia*. *Id.* at 470-71, 463 N.E.2d at 9, 474 N.Y.S.2d at 693. For a discussion contrasting the *Garcia* and *Perez* opinions, see Note, *The Resolution of Act of State Disputes Involving Indefinitely Situated Property*, 25 VA. J. INT'L L. 901, 920-26 (1985).

75. *Braka v. Bancomer, S.N.C.*, 762 F.2d 222 (2d Cir. 1985); *Callejo v. Bancomer, S.A.*, 764 F.2d 1101 (5th Cir. 1985).

76. For an overview of the development of the Mexican economic crisis, see 4 A. LOWENFELD, *THE INTERNATIONAL MONETARY SYSTEM* § 9.61 (2d ed. 1984). See also Hoagland, *Overview: Perspective from an American Lawyer in Mexico*, 18 INT'L LAW. 287 (1984); Tapia, *Mexico's Debt Restructuring: The Evolving Solution*, 23 COLUM. J. TRANSNAT'L L. 1 (1984); Zamora, *Peso-Dollar Economics and the Imposition of Foreign Exchange Controls in Mexico*, 32 AM. J. COMP. L. 99 (1984).

77. See 4 A. LOWENFELD, *supra* note 76, § 9.61. The Mexican Ministry of the Treasury and Public Credit issued the first decree in August 1983. *Id.*

The "special exchange rate" provided fewer pesos per dollar than the prevailing free market rate. See *id.* Professor Lowenfeld demonstrated the effect of this special exchange rate by discussing a situation in which the prescribed exchange rate was 69.5 pesos per dollar:

Purchase of dollars was not forbidden. But if a person had a 10,000 dollar account at a bank in Mexico and needed dollars, he would be entitled to withdraw 695,000 pesos; he could then take the pesos to the foreign exchange market and if dollars were available he could purchase them at the market rate of, say 100 pesos to the dollar, so that he would wind up with U.S. \$6,950, a 30 percent loss.

Id. § 9.61 n.j (citations omitted).

78. See, e.g., *Wolf v. Banco Nacional de Mexico, S.A.*, 739 F.2d 1458 (9th Cir. 1984), *cert. denied*, 105 S. Ct. 784 (1985); *Braka v. Bancomer, S.A.*, 589 F.

In *Braka v. Bancomer, S.N.C.*,⁷⁹ plaintiffs sought to recover 900,000 dollars lost as a result of the artificial exchange rate prescribed by the Mexican government.⁸⁰ In considering whether the act of state doctrine applied, the Second Circuit focused on the situs of the property in question, which it deemed to be "Bancomer's obligation to pay the contractually mandated return on plaintiffs' investment."⁸¹ Instead of relying on its approach in *Garcia*,⁸² the Second Circuit invoked the *Tabacalera* or *fait accompli* theory of situs analysis⁸³ and held that the actions by the Mexican government were an accomplished act with respect to the property.⁸⁴ The *Braka* court found that the situs of intangible property had been "contractually mandated" because the certificates of deposit named Mexico City as the place of deposit and as the place for payment of the principal and interest.⁸⁵ The *Braka* court reasoned, therefore, that the Mexican government "Ha[d] the parties and the *res* before it and act[ed] in such a manner as to change the relationship between the parties touching the *res*," so that the Mexican act was a *fait accompli*.⁸⁶ Thus, the court concluded that since the Mexican decrees affected property located within Mexican territory, the act of state doctrine barred

Supp. 1465 (S.D.N.Y. 1984), *aff'd*, 762 F.2d 222 (2d Cir. 1985); *Braka v. Multibanco Comermex, S.A.*, 589 F. Supp. 802 (S.D.N.Y. 1984).

79. 762 F.2d 222 (2d Cir. 1985).

80. *Id.* at 223. At the time the plaintiffs in *Braka* purchased the certificates of deposit, the defendant, Bancomer, was a privately run Mexican bank. *Id.* In September 1982, Mexico issued decrees nationalizing Mexican banks, including Bancomer. *Id.* The officially prescribed exchange rate at issue in *Braka* was approximately 70-80 pesos per dollar while the actual market rate of exchange was 135-150 pesos per dollar. *Id.*

The United States District Court for the Southern District of New York dismissed the plaintiffs' case on the basis of the act of state doctrine. *Braka v. Bancomer, S.A.*, 589 F. Supp. 1465, 1471 (S.D.N.Y. 1984).

81. 762 F.2d at 224.

82. *Id.* at 225 (citing *Garcia*, 735 F.2d at 646, 650). For a discussion of the *Garcia* case, see *supra* notes 66-74 and accompanying text. The *Braka* court distinguished the *Garcia* case, noting that in *Garcia* the certificates specified that repayment could be made at any branch worldwide, while in *Braka* the certificates were payable only in Mexico; therefore, the situs of debt in *Braka* existed wholly within the boundaries of Mexico. 762 F.2d at 225 (citing *Garcia*, 735 F.2d at 646, 650).

83. 762 F.2d at 224-25 (citing *Tabacalera*, 392 F.2d at 715-16). For a discussion of the *Tabacalera* case and its situs analysis, see *supra* notes 57-65 and accompanying text.

84. 762 F.2d at 224.

85. *Id.* Plaintiffs argued that the debt was located in New York because several purchases of certificates were made by tendering checks to Bancomer's New York agency and because the plaintiffs received some interest payments in New York. *Id.* The *Braka* court rejected this argument, stating: "It is clear that the accomplishment of interbank transfers, which was the extent of the New York agency's participation, does not change the contractually mandated situs of plaintiffs' property." *Id.* at 224-25.

86. *Id.* at 225 (brackets supplied by the court) (quoting *Tabacalera*, 392 F.2d at 715).

recovery.⁸⁷

In *Callejo v. Bancomer, S.A.*,⁸⁸ a case involving virtually the same facts as *Braka*, the Fifth Circuit also found the act of state doctrine applicable after concluding that the situs of the property was Mexico.⁸⁹ The *Callejo* court, however, explicitly rejected the *fait accompli* test, which it had formulated in *Tabacalera*, as a means of determining the situs of the deposits.⁹⁰ The court reasoned that the *fait accompli* test was designed for suits involving attempts by a foreign government to collect a debt rather than attempts to avoid payment of debt.⁹¹ The court stated:

If we simply apply the *Tabacalera* test, the situs of the certificates would clearly be Mexico, since Mexico can enforce the collection of debts owed by Bancomer, a Mexican domiciliary. In that event, the act of state doctrine would apply whenever a foreign state seized debts owed by its banks, no matter how many ties the debts had to this country.

We do not think *Tabacalera* intended such results.⁹²

87. *Id.* at 225-26.

88. 764 F.2d 1101 (5th Cir. 1985).

89. *Id.* at 1125. Beginning in 1979 or 1980, William and Adelfa Callejo, United States citizens, purchased certificates of deposit from defendant Bancomer, a then privately run Mexican bank. *Id.* at 1105. The four certificates of deposit at issue were denominated in United States dollars and specified Mexico City as the place of payment. *Id.* at 1106. Following the enactment of the Mexican exchange control regulations, the Callejos' certificates were payable in pesos at a rate substantially below the market rate. *Id.* As a result, the Callejos renewed two of the certificates due in August 1982 and filed the present suit. *Id.*

The *Callejo* court addressed three issues in addition to the act of state defense. First, the court concluded that Bancomer was not entitled to immunity under the Foreign Sovereign Immunities Act. *Id.* at 1106-12. For a discussion of the Foreign Sovereign Immunities Act, see *supra* note 6. Second, the court found that were it to adopt the commercial activity exception to the act of state doctrine, the exception would not apply in *Callejo* since the activity in question, Mexico's promulgation of exchange controls, was a government act. 764 F.2d at 1114-16. For a discussion of the commercial activity exception, see *supra* note 46. Third, the court examined whether the treaty exception to the act of state doctrine was applicable. 764 F.2d at 1116-21. In particular, the plaintiff alleged that the International Monetary Fund Articles of Agreement (Bretton Woods Agreement) constituted a treaty that was violated by the Mexican exchange control regulations. *Id.* at 1117-18. The court found it unnecessary to rule on this issue since the International Monetary Fund indicated that the Mexican regulations were consistent with the Bretton Woods Agreement. *Id.* at 1119. For a discussion of the potential applicability of the Bretton Woods Agreement to such cases, see *infra* notes 141-44 and accompanying text.

90. 764 F.2d at 1122-23 (citing *Tabacalera*, 392 F.2d at 715). For a discussion of *Tabacalera*, see *supra* notes 57-65 and accompanying text.

91. 764 F.2d at 1123.

92. *Id.* (citations omitted). The court added:

The power to collect a debt is for the benefit of the creditor, not the debtor; the fact that a debt can be enforced by the creditor in one forum should not be the basis of depriving him of his ability to enforce the debt in a different forum. Otherwise, the sword of the creditor

Citing *Garcia*, the court determined the location of the intangible property by examining the "incidents of the debt."⁹³ In this analysis, the court considered that the certificates were issued and carried by a Mexican bank, and called for payment in Mexico.⁹⁴ The court concluded that the certificates were located in Mexico, and that therefore the act of state doctrine defeated the plaintiff's claims against the Mexican banks.⁹⁵

Under any of the foregoing situs tests, a finding that property is located in the United States bars application of the act of state doctrine, but it does not necessarily preclude judicial recognition of the foreign sovereign's acts. Several courts have recognized extraterritorial acts of state that are consistent with United States law and policy.⁹⁶ For exam-

would become a shield for the debtor. Since we do not believe that debts owed by foreign banks to American nationals are always situated in the foreign country—and consequently do not believe that the act of state doctrine always applies to such debts—we do not apply the *Tabacalera* test here.

Id. (citations omitted).

93. *Id.* at 1123-24 & 1123 n.31 (citing *Garcia*, 735 F.2d at 650). The *Callejo* court also cited the following cases as support for its "incidents of the debt" test: *Allied Bank Int'l v. Banco Credito Agrícola de Cartago*, 757 F.2d 516, 521 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985); *Libra Bank Ltd. v. Banco Nacional de Costa Rica*, 570 F. Supp. 870, 881-82 (S.D.N.Y. 1983); *Weston Banking Corp. v. Turkiye Govanti Bankasi*, 57 N.Y.2d 315, 442 N.E.2d 1195, 456 N.Y.S.2d 684 (1982). *Callejo*, 764 F.2d at 1123 n.31.

In applying the incidents of the debt test, the *Callejo* court identified the following factors: (1) the place where the certificates were issued and are carried; (2) the place of payment; (3) "the intent of the parties . . . regarding the applicable law"; and (4) "the involvement of the American banking system in the transaction." 764 F.2d at 1123 (footnote omitted). The court's determination that the certificates were sited in Mexico was based on two of these four factors—that the certificates were issued and payable in Mexico. *Id.* at 1124.

94. 764 F.2d at 1124.

95. *Id.* at 1125.

96. See RESTATEMENT (Revised), *supra* note 19, § 469 reporter's note 4; Zaitzeff & Kunz, *supra* note 49, at 461-64. See also *Banco Nacional de Cuba v. Chemical Bank N.Y. Trust Co.*, 658 F.2d 903, 908-09 (2d Cir. 1981); *United Bank Ltd. v. Cosmic Int'l, Inc.*, 542 F.2d 868, 872 (2d Cir. 1976); *Menendez v. Saks & Co.*, 485 F.2d 1355, 1364 (2d Cir. 1973), *rev'd on other grounds sub nom. Alfred Dunhill, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976); *Republic of Iraq v. First City Nat'l Bank*, 353 F.2d 47, 51 (2d Cir. 1965), *cert. denied*, 382 U.S. 1027 (1966); *F. Palicio y Compania, S.A. v. Brush*, 256 F. Supp. 481, 487-88 (S.D.N.Y. 1966), *aff'd per curiam*, 375 F.2d 1011 (2d Cir.), *cert. denied*, 389 U.S. 830 (1967). *Cf. United States v. Pink*, 315 U.S. 203 (1942); *United States v. Belmont*, 301 U.S. 324 (1937). *Belmont* and *Pink* both involved the Soviet Union's nationalization of property located in the United States that was owned by Soviet citizens. See, e.g., *Pink*, 315 U.S. at 210-11. The Soviet Union signed an executive agreement with the United States (the Litvinov Assignment) under which the United States agreed to recognize and make claims pursuant to the Soviet Nationalization decrees confiscating property in New York. *Id.* at 211-13. Based on the Litvinov Assignment, the Court in *Pink* recognized the validity of the confiscatory decrees which in the absence of an executive agreement may not have been

ple, in *Republic of Iraq v. First National City Bank*,⁹⁷ the Second Circuit, after first deciding that an Iraqi ordinance was not within the act of state doctrine,⁹⁸ examined whether the ordinance was consistent with United States law and policy,⁹⁹ reasoning that if the ordinance were consistent, the court would give it extraterritorial recognition.¹⁰⁰

B. *The Bernstein Exception*

The *Bernstein* exception to the act of state doctrine draws its name from two Second Circuit decisions—*Bernstein v. Van Heyghen Freres Societe Anonyme*¹⁰¹ and *Bernstein v. N.V. Nederlandsche-Amerikaansche Stoomvaart-Maatschappij*.¹⁰² In these cases, the plaintiff sought to recover the value of a shipping vessel that he had transferred to the Nazi government under duress during World War II.¹⁰³ Although the Nazi seizure fell within the scope of the act of state doctrine, the Second Circuit determined that the doctrine was inapplicable in situations where the executive branch clearly indicated that it did not object to judicial examination of the acts of a foreign state.¹⁰⁴ Finding no such indication in the first *Bernstein* case, the Second Circuit applied the act of state doctrine to the Nazi seizure.¹⁰⁵ In the second *Bernstein* case, the Second Circuit relied on a letter from the acting legal adviser to the State Department to avoid application of the act of state doctrine.¹⁰⁶ The State Department's letter

recognized since they may have been viewed as confiscations against the law and policy of the United States. See Note, *supra* note 74, at 930 n.147.

97. 353 F.2d 47 (2d Cir. 1965), *cert. denied*, 382 U.S. 1027 (1966). For a discussion of the facts in *Republic of Iraq*, see *supra* note 55.

98. 353 F.2d at 50-51. The court noted that traditionally the act of state doctrine "applies only to a taking by a foreign sovereign of property within its own territory." *Id.* at 51.

99. *Id.* at 51-52.

100. *Id.* at 51. The court, however, found the ordinance inconsistent since it amounted to a confiscation "contrary to our public policy and shocking to our sense of justice." *Id.* (citing *Vladikavkazsky Ry. v. N.Y. Trust Co.*, 263 N.Y. 369, 378, 189 N.E. 456, 460 (1934)).

101. 163 F.2d 246 (2d Cir.), *cert. denied*, 332 U.S. 772 (1947).

102. 173 F.2d 71 (2d Cir. 1949), *modified per curiam*, 210 F.2d 375 (1954). After plaintiff *Bernstein's* first case was dismissed, he brought this separate action against another defendant. 173 F.2d at 72.

103. See *Bernstein v. Van Heyghen Freres Societe Anonyme*, 163 F.2d at 247. The Nazi government sold the vessel to a Belgian company during World War II. *Id.* The vessel was sunk during the war and insurance proceeds of 100,000 pounds were paid to another Belgian company which held these proceeds in the defendant's account. *Id.* The plaintiff attempted to attach this debt by filing his complaint in federal district court in New York. *Id.*

104. *Id.* at 248-51. Judge Learned Hand stated: "the only relevant consideration is how far our Executive has indicated any positive intent to relax the doctrine that our courts shall not entertain actions of the kind at bar; some positive evidence of such an intent being necessary." *Id.* at 251.

105. *Id.* at 251-52.

106. *Bernstein v. N.V. Nederlandsche-Amerikaansche Stoomvaart-Maatschappij*, 210 F.2d 375, 376 (2d Cir. 1954) (*per curiam*).

announced the policy of the executive to relieve United States courts from any restraints on their ability to adjudicate confiscatory acts by the Nazi government.¹⁰⁷

The Supreme Court most recently assessed the *Bernstein* exception in *First National City Bank v. Banco Nacional de Cuba*,¹⁰⁸ a case that left the viability of the exception uncertain. Justice Rehnquist, writing for the plurality and joined by Chief Justice Burger and Justice White, wholly approved of the *Bernstein* exception.¹⁰⁹ He reasoned that where the executive indicates approval of judicial resolution, the rationale of giving deference to the political branch in matters of foreign policy ceases to be viable.¹¹⁰ Six Justices, however, disapproved of the *Bernstein* exception.¹¹¹ Justice Douglas, in a concurring opinion, asserted that under the *Bernstein* exception the Court would become handmaiden for the ex-

107. *Id.* The letter as quoted in the court's opinion stated in part:

1) This Government has consistently opposed the forcible acts of dispossession of a discriminatory and confiscatory nature practiced by the Germans on the countries or peoples subject to their controls. . . .

3) The policy of the Executive, with respect to claims asserted in the United States for the restitution of identifiable property . . . lost through force, coercion, or duress as a result of Nazi persecution in Germany, is to relieve American courts from any restraint upon the exercise of their jurisdiction to pass upon the validity of the acts of Nazi officials.

Id. Based on this expression of foreign policy, the court amended its earlier mandate that had precluded it from adjudicating the confiscatory acts of the Nazi government. *Id.* (citing 173 F.2d at 75-76).

108. 406 U.S. 759 (1972) (plurality opinion). In 1960, First National City Bank (First National) was owed \$10 million by the predecessor of Banco Nacional de Cuba (Banco Nacional). *Id.* at 760. This loan was secured by a pledge of United States Government bonds. *Id.* Subsequently, Castro nationalized all of First National's Cuban branches. *Id.* In retaliation, First National sold the United States bonds to satisfy the loan, with proceeds in excess of the debt by 1.8 million dollars. *Id.* at 760-61. Banco Nacional sued First National in a United States court to recover the excess proceeds; First National counterclaimed, asserting an action for damages resulting from the expropriation of its property by the Cuban government. *Id.* at 761. Banco Nacional claimed that the nationalization of First National's Cuban branches was an act of state that must be recognized by United States courts. *See id.* at 761. The legal adviser of the Department of State advised the Court that "where the Executive publicly advises the Court that the act of state doctrine need not be applied, the Court should proceed to examine the legal issues raised. . . ." *Id.* at 764. The legal advisor further asserted that there existed an exception to the act of state doctrine for counterclaims: "The Department of State believes that the act of state doctrine should not be applied to bar consideration of a defendant's counterclaim or set-off against the Government of Cuba in this or like cases." *Id.*

109. *Id.* at 768.

110. *Id.* Justice Rehnquist relied on a common law maxim that "[t]he reason of the law ceasing, the law itself also ceases." *Id.* (quoting BLACK'S LAW DICTIONARY 288 (4th ed. 1951)).

111. Justice Douglas concurred. *Id.* at 772 (Douglas, J., concurring). Justice Powell concurred. *Id.* at 773 (Powell, J., concurring). Justice Brennan, joined by Justices Stewart, Blackmun, and Marshall, dissented. *Id.* at 776-93 (Brennan, J., dissenting).

executive branch "which may choose to pick some people's chestnuts from the fire but not others'."¹¹² In a separate concurring opinion, Justice Powell expressed discomfort with an exception to the act of state doctrine that requires the Court to receive permission from the executive branch.¹¹³ Finally, in a lengthy dissenting opinion, Justice Brennan, joined by Justices Stewart, Marshall, and Blackmun, denounced the *Bernstein* exception on several grounds.¹¹⁴

Primarily, Justice Brennan noted that Justice Rehnquist's plurality opinion was premised on the theory that a court will not, by failure to apply the act of state doctrine, embarrass the executive branch if the executive branch has indicated its approval of nonapplication of the doctrine.¹¹⁵ Justice Brennan asserted that avoidance of embarrassment to the executive branch is only one policy justification for the act of state doctrine.¹¹⁶ Relying on *Sabbatino*, Justice Brennan urged that courts invoke the doctrine when there is a lack of consensus among nations as to the applicable rule of law.¹¹⁷ Additionally, Justice Brennan pointed out that the act of state doctrine recognizes the superior power of the Executive in the conduct of foreign affairs; for example, where a foreign government has affected mass expropriations, the executive branch and not the judiciary has power to ensure that all similarly situated plaintiffs are treated equally.¹¹⁸

112. *Id.* at 773 (Douglas J., concurring). Justice Rehnquist addressed this issue in his plurality opinion:

Our holding is in no sense an abdication of the judicial function to the Executive Branch. The judicial power of the United States extends to this case, and the jurisdictional standards established by Congress for adjudication by the federal courts have been met by the parties. The only reason for not deciding the case by use of otherwise applicable legal principles would be the fear that legal interpretation by the judiciary of the act of a foreign sovereign within its own territory might frustrate the conduct of this country's foreign relations. But the branch of the government responsible for the conduct of those foreign relations has advised us that such a consequence need not be feared in this case. The judiciary is therefore free to decide the case without the limitations that would otherwise be imposed upon it by the judicially created act of state doctrine.

Id. at 768 (plurality opinion).

113. *Id.* at 773 (Powell, J., concurring). Justice Powell observed: "I would be uncomfortable with a doctrine which would require the judiciary to receive the Executive's permission before invoking its jurisdiction. Such a notion, in the name of the doctrine of separation of powers, seems to me to conflict with that very doctrine." *Id.*

114. *Id.* at 776-93 (Brennan, J., dissenting).

115. *Id.* at 785-90 (Brennan, J., dissenting). For a discussion of Justice Rehnquist's plurality opinion, see *supra* notes 109-10 and accompanying text.

116. 406 U.S. at 785-90 (Brennan, J., dissenting).

117. *Id.* at 785-86 (Brennan, J., dissenting) (citing *Sabbatino*, 376 U.S. at 427-28)). For a discussion of *Sabbatino* and the justifications it established for applying the act of state doctrine, see *supra* notes 38-42 and accompanying text.

118. 406 U.S. at 786-87 (Brennan, J., dissenting). Justice Brennan quoted *Sabbatino*:

Notwithstanding the uncertain validity of the *Bernstein* exception following *First National City Bank*, the exception has resurfaced in subsequent lower court decisions.¹¹⁹ In the Second Circuit, suggestions from the executive branch, along with other factors, have been alluded to in cases involving the act of state doctrine; however, in each case, the court did not specify whether the executive suggestion controlled the applicability of the doctrine.¹²⁰

IV. *ALLIED BANK INTERNATIONAL V. BANCO CREDITO AGRICOLA DE CARTAGO*

In 1981, Costa Rica was burdened with an enormous foreign debt and with the effects of the worldwide recession, which had depressed the prices of coffee and bananas, its chief exports.¹²¹ In an effort to cope with the flight of foreign currency from its country, the Costa Rican government issued directives effectively prohibiting the payments of external debt with foreign currency.¹²² As a result of these directives, Costa

Following an expropriation of any significance, the Executive engages in diplomacy aimed to assure that United States citizens who are harmed are compensated fairly. Representing all claimants of this country, it will often be able, either by bilateral or multilateral talks, by submission to the United Nations, or by the employment of economic and political sanctions, to achieve some degree of general redress. Judicial determinations of invalidity of title can, on the other hand, have only an occasional impact, since they depend on the fortuitous circumstance of the property in question being brought into this country.

Id. at 787 (Brennan, J., dissenting) (quoting *Sabbatino*, 376 U.S. at 431).

119. *Banco Nacional de Cuba v. Chemical Bank N.Y. Trust Co.*, 658 F.2d 903, 911-12 (2d Cir. 1981); *Banco Nacional de Cuba v. Chase Manhattan Bank*, 658 F.2d 875, 881-85 (2d Cir. 1981). *Cf.* *First Nat'l Bank of Boston (Int'l) v. Banco Nacionl de Cuba*, 658 F.2d 895, 902 (2d Cir. 1981).

120. *See Banco Nacional de Cuba v. Chemical Bank N.Y. Trust Co.*, 658 F.2d 903 (2d Cir. 1981) (in addition to absence of executive suggestion, court considered that subject claim was based on breach of agreement, not on violation of international law; case remanded); *Banco Nacional de Cuba v. Chase Manhattan Bank*, 658 F.2d 875 (2d Cir. 1981) (in addition to executive suggestion, court noted that there was no showing that adjudication would "interfere with delicate foreign relations," as counterclaim did not exceed value of sovereign's claim; act of state doctrine was inapplicable). For a criticism of the *Bernstein* exception, see Note, *Acts of State and the Conflict of Laws*, 35 N.Y.U. L. REV. 234, 238-40 (1960). This commentator points out that executive suggestions have long been an acceptable means for the executive branch to intervene in a case, but asserts that such suggestions should not be determinative of the outcome of the case. *Id.* at 240 & n.44 (citing *Schooner Exchange v. McFaddon*, 11 U.S. (7 Cranch) 116 (1812)). *See also* Editorial Comment, *Has the Supreme Court Abdicated One of Its Functions?*, 40 AM. J. INT'L L. 168 (1946).

121. *See Canas, Costa Rica: Another View*, BARRON'S, July 5, 1982, at 36, col. 2. According to Canas, inflation in Costa Rica in 1982 was close to 90%, unemployment exceeded 20%, and foreign debt reached \$3.2 billion. *Id.* Approximately \$1.4 billion of Costa Rica's foreign debt was owed to private lenders; the majority were United States banks. *Id.* *See also* Kallen, *Yes, We Have No Bananas*, FORBES, July 1, 1985, at 97.

122. *See Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 566 F.

Rican banks were temporarily unable to make payments due on notes to foreign creditors, which prompted the creditors to sue the Costa Rican banks in the United States.¹²³

In *Allied Bank v. Banco Credito Agricola de Cartago*, Allied, a banking syndicate comprised of thirty-nine United States and European banks,¹²⁴ brought suit against three Costa Rican banks.¹²⁵ The district court concluded that the act of state doctrine was applicable since a judgment against the Costa Rican banks could potentially cause embarrassment to the executive branch in its relationship with the Costa Rican government.¹²⁶

Supp. 1440, 1442 (S.D.N.Y. 1983), *rev'd*, 757 F.2d 516 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985).

In August 1981, the Central Bank of Costa Rica (Central Bank), a government controlled bank, passed a resolution prohibiting public sector entities from paying principal or interest on external debt with foreign currency. 566 F. Supp. at 1442. In November 1981, the President of Costa Rica and the Ministry of Finance promulgated an executive decree which prohibited any institution in Costa Rica from making external payments on debts without approval from the Central Bank in consultation with the Ministry of Finance. *Id.*

123. See *Libra Bank Ltd. v. Banco Nacional de Costa Rica*, 570 F. Supp. 870 (S.D.N.Y. 1983); *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 566 F. Supp. 1440 (S.D.N.Y. 1983), *rev'd*, 757 F.2d 516 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985).

124. A syndicate is defined as "[a]n association of individuals, formed for the purpose of conducting and carrying out some particular business transaction, ordinarily of a financial character, in which the members are mutually interested." BLACK'S LAW DICTIONARY 1300 (5th ed. 1979).

Loans to foreign sovereigns and their instrumentalities are often made from a syndicate of banks rather than from a single banking institution. See *Clarke & Farrar*, *supra* note 4, at 229. The foreign borrower will typically seek out a principal United States bank to act as "manager" in arranging a syndicate of lenders. *Id.* Another principal bank will act as an "agent" for the syndicate with responsibilities for overseeing the flow of funds between the parties involved in the loan transaction. *Id.* at 230. The benefit of such an approach is that a foreign borrower can request more money than it could from any one private lender. *Id.* at 229.

125. See *Allied*, 566 F. Supp. at 1442. The three defendant Costa Rican banks were Banco Credito Agricola de Cartago, Banco Anglo Costarricense, and Banco Nacional de Costa Rica. *Id.* at 1440. At present, these banks are wholly owned by the government of Costa Rica and are subject to the direct control of the Central Bank of Costa Rica. See *id.* at 1441-42.

While this action was still pending in the district court, the Costa Rican government initiated negotiations for the rescheduling of the defendant banks' obligations to the Allied Syndicate. *Allied I*, *supra* note 10, at 745. Thereafter, an agreement was reached between the defendant banks and all but one of the 39 banks in the Allied Syndicate. *Id.* One bank, Fidelity Union Trust Company of New Jersey, refused to enter into the agreement and on behalf of it alone, Allied pressed the subsequent appeal of the case. *Id.* The Costa Rican banks nevertheless proceeded to make payments to the other thirty-eight banks under this refinancing agreement. *Id.* For a further discussion of the settlement, see *infra* notes 193-96 and accompanying text.

126. 566 F. Supp. at 1444. District Judge Griesa determined that Costa Rica imposed the directive in response to a serious national economic crisis; therefore, a judicial determination in favor of Allied would put the judicial

On the first appeal (*Allied I*),¹²⁷ the Second Circuit affirmed the district court's decision; however, it did not reach the issue of whether the act of state doctrine was applicable.¹²⁸ The *Allied I* court analyzed whether it should uphold the Costa Rican directives based on their consistency with United States law and policy.¹²⁹

branch at odds with the Costa Rican government on a matter of central importance to Costa Rica and hence risk embarrassment in the executive branch's relationship with Costa Rica. *Id.* at 1443-44.

Within days of the district court decision in *Allied*, Chief Judge Motley ruled on *Libra Bank Ltd. v. Banco Nacional de Costa Rica*, a case involving virtually the same facts as *Allied*, and reached an opposite conclusion regarding the act of state doctrine. 570 F. Supp. 870, 884 (S.D.N.Y. 1983).

The *Libra* court concluded that applicability of the act of state doctrine turned on whether the debt was located in Costa Rica. *Id.* at 878. The court noted that the test employed in the Second Circuit for determining the situs of intangible property focused on whether the sovereign could enforce the payment of the debt. *Id.* at 880-81. The court, however, concluded that this approach was not applicable to the facts of *Libra* since it was designed for cases involving an attempt by a foreign sovereign to confiscate debts owed by a *United States national*. *Id.* The *Libra* facts involved just the opposite—a debt owed by a *foreign national* to a United States bank. *Id.*

In place of the "enforcement" test the court focused on the "legal incidents" of the debt in order to site the debt. *Id.* at 881-82 (citing *Weston Banking Corp. v. Turkiye Garanti Bankasi*, 57 N.Y.2d 315, 442 N.E.2d 1195, 456 N.Y.S.2d 684 (1982)). For a discussion of the "legal incidents" test for siting intangible property, see *supra* notes 93-95 and accompanying text. Chief Judge Motley concluded that at the time Costa Rica promulgated its directives the situs of the debt was New York, based on the following "legal incidents": (1) Banco Nacional consented to jurisdiction in the United States; (2) it agreed to have the loan documents construed in accordance with New York law; (3) it agreed to make payments in New York; (4) it agreed to make payments as provided in the promissory notes irrespective of any charges or withholdings imposed in connection with the notice; and (5) it owned considerable assets in the United States. 570 F. Supp. at 881-82.

After determining that the act of state doctrine was not applicable, the court noted that it would only give extraterritorial effect to the Costa Rican directives if they were consistent with United States law and policy. *Id.* at 882. The court found that the directives confiscated property without adequate compensation, and as such, were repugnant to the United States Constitution. *Id.* The *Libra* court also rejected the defendant's argument that nonenforcement of the loan agreement was permitted by article VIII, § 2(b), of the Bretton Woods Agreement. *Id.* at 896-902 (memorandum opinion denying defendant's motion for reargument of plaintiff's summary judgment motion). For a discussion of the potential application of this provision in cases involving transactions with debtor countries, see *supra* note 12. The *Libra* court granted summary judgment in favor of the United States creditors. 570 F. Supp. at 896.

127. *Allied I*, *supra* note 10. The panel for *Allied I* and *Allied II* comprised Judges Meskill and Pierce with Judge Metzner, United States District Judge for the Southern District of New York, sitting by designation. *Id.* at 743; *Allied Bank Int'l v. Banco Credito Agricola de Cartago*, 757 F.2d 516, 518 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985).

128. *Allied I*, *supra* note 10, at 745-46.

129. *Id.* at 746. For a discussion of the principle of comity, see *supra* notes 30-39 and accompanying text. Although the court labeled this a "comity" analysis, the court's analysis was actually more in line with the law and policy analysis

The court applied this "comity" analysis rather than an act of state analysis because it deemed the question of whether the directives were consistent with United States law and policy to be controlling.¹³⁰ The court reasoned that the act of state doctrine would apply only if the debts were located in Costa Rica.¹³¹ If, however, the debts' situs was the United States, the directives could still be recognized by the court if they were consistent with United States law and policy.¹³² The court therefore concluded that the act of state doctrine did not control.¹³³

In finding the Costa Rican directives consistent with United States law and policy, the *Allied I* court principally relied on an analogy to United States bankruptcy law.¹³⁴ In support of this analogy, the court relied on *Canada Southern Railway v. Gebhard*¹³⁵ in which the Supreme Court held that United States citizens who owned bonds issued by Canada Southern Railway, a governmentally owned corporation, were required to adhere to Canada's reorganization of the railway's debt.¹³⁶

performed in past Second Circuit cases where the act of state doctrine was deemed inapplicable. For a discussion of this "second step" taken in prior act of state cases, see *supra* notes 96-100 and accompanying text.

130. *Allied I*, *supra* note 10, at 745-47.

131. *Id.* at 746.

132. *Id.*

133. *See id.*

134. *Id.* The court found several other factors indicating that the Costa Rican directives were consistent with United States law and policy. *See id.* at 744-46. The court first noted that even though Costa Rica had defaulted on inter-governmental loans with the United States, the Reagan Administration had indicated its continuing support and its commitment to provide economic assistance to Costa Rica. *Id.* at 745. The court quoted the following advice from the executive branch:

Continuation of U.S. assistance to Costa Rica is consistent with the commitment of this Administration and in Congress to help Costa Rica regain economic viability. We therefore regard such assistance, which is designed to help the Government with financial and management reforms and with needed credit to the private sector, as vital and in the national interest. We are hopeful that bilateral debt restructuring will be completed within the next several months.

Id. (quoting Letters from Secretary of State George P. Schultz to Speaker of the House Thomas P. O'Neill (Mar. 18, 1983 & Oct. 11, 1983)). Further, the court noted that the House of Representatives expressed support for Costa Rica "as that country responds to the current economic crises." *Id.* (citing H.R. Con. Res. 423, 97th Cong., 2d Sess., 128 CONG. REC. 10,206 (1982); H.R. Con. Res. 194, 98th Cong., 1st Sess. 129 CONG. REC. 10,350 (1983)). Finally, the court noted a Paris Club Agreed Minute that supported the restructuring of Costa Rica's external debt. *Id.* The Paris Club is an informal organization of creditor countries, including the United States, which periodically meets under the chairmanship of an official of the French treasury to set forth guidelines for rescheduling the debts of a country seeking relief. *See generally* Rieffel, *The Paris Club, 1978-1983*, 23 COLUM. J. TRANSNAT'L L. 83 (1984) (discussing history, objectives, and procedures of Paris Club).

135. 109 U.S. 527 (1883).

136. *Allied I*, *supra* note 10, at 746 (citing *Gebhard* 109 U.S. 527 (1883)). The *Allied I* court relied on the following reasoning in *Gebhard*:

The *Allied I* court compared the *Gebhard* situation to the Costa Rican directives and extended the court's reasoning in *Gebhard* to chapter 11 of the United States Bankruptcy Code, which automatically stays all collection actions against a party that has filed an application for reorganization.¹³⁷ The *Allied I* court concluded that Costa Rica, like a petitioner in bankruptcy, acted in good faith in attempting to defer its payments while renegotiating its debt; therefore, its directives were consistent with United States law and policy.¹³⁸

On rehearing (*Allied II*), the same panel of judges¹³⁹ reversed and vacated its earlier decision.¹⁴⁰ Based on views articulated by the executive branch in an amicus curiae brief, the *Allied II* court concluded that the directives were inconsistent with United States law and policy.¹⁴¹ The *Allied II* court noted that the amicus brief urged that United States policy does not support a unilateral decision by a debtor nation to

[The plan] is in entire harmony with the spirit of bankrupt laws, the binding force of which, upon those who are subject to the jurisdiction, is recognized by all civilized nations. It is not in conflict with the Constitution of the United States, which . . . allows Congress "to establish . . . uniform laws on the subject of bankruptcy throughout the United States." . . . Under these circumstances the true spirit of international comity requires that schemes of this character, legalized at home, should be recognized in other countries.

Id. (quoting *Gebhard*, 109 U.S. at 539).

137. *Allied I*, *supra* note 10, at 746 (citing 11 U.S.C. §§ 103(a), 362, 901(a) (1982)).

138. *Id.* at 746-47. For a discussion of Costa Rica's renegotiation efforts, see *infra* notes 192-96 and accompanying text.

139. See *supra* note 127.

140. *Allied Bank Int'l v. Banco Credito Agrícola de Cartago (Allied II)*, 757 F.2d 516, 519-20 (2d Cir.), *cert. dismissed*, 106 S. Ct. 30 (1985).

141. 757 F.2d at 519-20. The executive branch filed an amicus curiae brief urging reversal of the *Allied I* decision. *Id.* Of counsel on the brief were the State Department, the Department of Treasury, the Board of Governors of the Federal Reserve System, and the Justice Department. Brief for the United States as *Amicus Curiae*, *Allied II*, 757 F.2d 516 (on file at office of *Villanova Law Review*).

An amicus curiae brief urging reversal of *Allied I* also was filed by the New York Clearing House Association. Brief for the New York Clearing House Association as *Amicus Curiae*, *Allied II*, 757 F.2d 516 (on file at office of *Villanova Law Review*). The New York Clearing House Association is an association of twelve leading New York City banks which appears as *amicus curiae* before appellate courts in cases involving important questions pertinent to banking. *Id.* at 2. An amicus brief was also filed jointly by the Rule of Law Committee and the National Foreign Trade Council. Brief for the Rule of Law Committee and the National Foreign Trade Council, Inc. as *Amici Curiae*, *Allied II*, 757 F.2d 516 (on file at office of *Villanova Law Review*). "The Rule of Law Committee is an informal, voluntary association of legal representatives from major American multinational corporations engaged in worldwide export, banking, petroleum manufacturing, and construction activities." *Id.* at 1. The National Foreign Trade Council is a nonprofit corporation concerned with international trade and investment; corporate membership of the council accounts for over 70% of all United States exports and United States foreign direct private investment. *Id.*

restructure its obligations.¹⁴² Instead, the Government's amicus brief indicated that the executive supports the International Monetary Fund (IMF)¹⁴³ restructuring procedure, which encourages cooperative and multilateral adjustment of international debt problems.¹⁴⁴

The court proceeded to address the act of state defense raised by the defendant Costa Rican banks, stating that application of the act of state doctrine to the facts in *Allied* depended on the situs of the debt at the time the Costa Rican directives were promulgated.¹⁴⁵

The court concluded that the determination of the situs of a debt is different for act of state purposes than it is for "ordinary" purposes.¹⁴⁶ Relying on the *fait accompli* theory set forth in *Tabacalera* for its act of state situs analysis,¹⁴⁷ the *Allied II* court concluded that since Costa Rica could not "wholly extinguish" the Costa Rican banks' obligation to timely pay United States dollars to Allied in New York, the situs of the debt was not Costa Rica.¹⁴⁸

The court also applied an "ordinary" situs analysis and again concluded that the situs of the debt was not Costa Rica.¹⁴⁹ The court's "ordinary" situs test involved a balancing of the interests of the United States against the interests of Costa Rica in siting the debt within its

142. 757 F.2d at 519.

143. *Id.* at 519. For a discussion of the International Monetary Fund, see *supra* note 12.

144. 757 F.2d at 519. The brief for the United States as amicus curiae stated:

Debtor countries have generally developed economic adjustment programs approved by the IMF, while financing by the IMF and others has been provided to ease the pace at which the adjustment must be accomplished. The IMF . . . has served as an objective mediator in the establishment of external financing requirements, and accordingly has frequently been a catalyst in mobilizing the financing essential to the viability of these programs. . . . United States policy has been strongly supportive of this approach to resolve the current international debt problem.

Brief for the United States as *Amicus Curiae* at 9-10, *Allied II*, 757 F.2d 516 (footnote omitted).

145. 757 F.2d at 520-22. The court initially observed that application of the act of state doctrine depends on the degree of impact a judicial decision would have on international relations. *Id.* at 520-21 (citing *Sabbatino*, 376 U.S. at 427-28, 431-33). Also, the court noted that it may be guided by a foreign policy viewpoint that has been articulated by the executive. 757 F.2d at 521 n.2. However, the court recognized that the act of state doctrine is "ultimately and always" a judicial doctrine, and thus an executive articulation cannot be wholly determinative. *Id.* Referring to the constitutional underpinnings of the doctrine, the court further stated that a judicial decision should not have the effect of embarrassing the executive in the conduct of foreign affairs. *Id.* at 521.

146. *Id.* at 521.

147. For a discussion of the *fait accompli* test for siting intangible property, see *supra* notes 57-65 and accompanying text.

148. 757 F.2d at 521 (citing *Tabacalera*, 392 F.2d at 715-16).

149. *Id.*

territory.¹⁵⁰ The court concluded that under both the *fait accompli* and "ordinary" situs analyses, the situs of the Costa Rican bank debt was the United States, and therefore, the act of state doctrine was inapplicable.¹⁵¹

Having rejected the Costa Rican banks' act of state defense, the *Allied II* court analyzed whether international comity would support recognition of the Costa Rican directives by a United States court.¹⁵² The court repeated its earlier analysis which found the Costa Rican directives contrary to the IMF debt resolution strategy.¹⁵³ Additionally, the court found that judicial recognition of the directives would be contrary to United States contract law.¹⁵⁴ Specifically, the Costa Rican banks had agreed, as an express term of the loan contract, that their repayment obligation would not be excused by a failure of the Costa Rican Central Bank to make available the necessary United States dollars for repayment.¹⁵⁵ The court concluded that to give effect to the Costa Rica directives would vitiate this express provision of the contract.¹⁵⁶ Based on the foregoing, the *Allied II* court directed the district court to enter judgment for Allied.¹⁵⁷

V. ANALYSIS

A. *The Questionable Utility of the Territorial Limitation to Cases Involving Intangible Property*

In *Allied II*, the court's act of state analysis centered upon the situs of the Costa Rican bank debts.¹⁵⁸ On its face, this approach appears to

150. *See id.* at 521-22. Under this "ordinary" situs analysis, the court balanced several factors that supported siting the debt in New York and ruled that those factors outweighed Costa Rica's interest in the contracts at issue. *Id.* The "New York" factors included: Costa Rica's consent to jurisdiction in the United States; Costa Rica's agreement to pay the loans in New York in United States dollars; and the United States' interest in maintaining New York's status as a financial center. *Id.* The court also noted that Allied Bank, the syndicate's agent, was located in New York. *Id.*

151. *Id.* at 522.

152. *Id.*

153. *Id.*

154. *Id.*

155. *Id.* The court quoted the pertinent terms of the Costa Rican loan agreement:

If the Borrower shall not effect any payment of principal or interest on the promissory notes at maturity, due solely to the omission or refusal by the Central Bank of Costa Rica to provide the necessary U.S. Dollars, such an event shall not be considered to be an event of default which would justify the demandability of the obligation, during a period of 10 days after such maturity date.

Id. at 522 n.4.

156. *Id.* at 522.

157. *Id.* at 523.

158. *See id.* at 521-22.

be proper since the act of state doctrine, under its traditional definition, is applicable only to a sovereign's acts done "within its own territory."¹⁵⁹ However, problems exist because the situs of intangible property is a fiction. It is submitted that when a court applies a situs test to intangible property, it is undertaking an arbitrary analysis that neglects the policies underlying the act of state doctrine.¹⁶⁰

A primary reason that courts devise "situs tests" is to provide some predictability as to the applicability of the act of state doctrine to international business transactions. This goal, however, has not been accomplished with respect to intangible property because courts disagree over the applicable test and the proper analysis under each test. To illustrate: In *Allied II* and *Braka*, the Second Circuit ignored its earlier situs tests and applied the Fifth Circuit's *fait accompli* test.¹⁶¹ Additionally, in *Allied II* the Second Circuit applied what it labeled an "ordinary" situs test along with the *fait accompli* test.¹⁶² In contrast, the Fifth Circuit, in *Callejo*, rejected the *fait accompli* test altogether as a means to site intangible property where a foreign national is the debtor and a United States

159. *Sabbatino*, 376 U.S. at 428. For a discussion of the territorial limitation of the act of state doctrine, see *supra* notes 49-97 and accompanying text.

160. See RESTATEMENT (REVISED), *supra* note 19, § 469 reporter's note 4. This note provides:

In principle, it might be preferable to approach the question of the applicability of the act of state doctrine to intangible assets not by searching for an imaginary situs for property that has no real situs, but by determining how the act of the foreign state in the particular circumstances fits within the reasons for the act of state doctrine and for the territorial limitation.

Id. (citations omitted).

For criticisms of the application of the territorial limitation to intangible property, see Henkin, *The Foreign Affairs Powers of the Federal Courts*: *Sabbatino*, 64 COLUM. L. REV. 805, 828 (1964) (if basis of act of state doctrine is related to foreign affairs, courts may not be competent to render decisions regarding sovereign acts that have impact outside sovereign's territory as well as within); Hoffman & Deming, *The Role of the U.S. Courts in the Transnational Flow of Funds*, 17 N.Y.U. J. INT'L L. & POL. 493, 494-95 (1985) (courts involved with debtor country litigation have become "mesmerized by such vestigial . . . concepts as the situs of an intangible debt . . . [and] . . . end up exacerbating the problems created by the debt crisis rather than contributing to a solution"); Lowenfeld, *In Search of the Intangible: A Comment on Shaffer v. Heitner*, 53 N.Y.U. L. REV. 102, 123 (1978) (mechanical situs tests do not serve values underlying act of state doctrine); Rosenthal, *Jurisdictional Conflicts Between Sovereign Nations*, 19 INT'L LAW. 487 (1985) (proposing that territorial limitation be replaced by limiting act of state doctrine to sovereign acts that effect sovereign's public policy within its territory); Comment, *supra* note 31, at 490-91 ("[a]n approach comprehensive enough to cover intangible as well as tangible property interests would go far to alleviate the confusion courts have experience [sic] in applying the doctrine"); Note, *supra* note 74, at 906-07 (courts can manipulate situs rules to reach any result they desire).

161. For a discussion of *Allied II*, see *supra* notes 139-57 and accompanying text. For a discussion of *Braka*, see *supra* notes 79-87 and accompanying text.

162. *Allied II*, 757 F.2d at 521-22.

national is the creditor.¹⁶³ The Fifth Circuit held that the *fait accompli* test was improper because any seizure of debts by a sovereign would always satisfy the test regardless of how many "ties" the loan contract had with the United States.¹⁶⁴

The Fifth Circuit's reasoning in *Callejo* necessarily implies that application of its *fait accompli* test in *Allied II* and *Braka* was inappropriate and that, moreover, even were the test applicable, the *Allied II* court reached the wrong conclusion under the test. The Fifth Circuit in *Callejo* set forth a situs test based on evaluating the "incidents" of a debt, a test comparable to the *Allied II* "ordinary" situs test, as well as to the approach taken by the Second Circuit in *Garcia*.¹⁶⁵ This apparent confusion among courts over the applicable situs test for intangible property has eroded any predictability in the application of the act of state doctrine to intangible property. As the law currently stands, parties to international loan transactions cannot know what test will determine the situs of the debt.

Further, the Second Circuit has not been consistent in its analysis under the *fait accompli* test. While in both *Allied II* and *Braka*, the court applied this test, its focus was different in each case. The *fait accompli* test originally revolved on whether the act of the foreign state came "to complete fruition" within the borders of the acting sovereign.¹⁶⁶ In *Allied II*, the court reasoned that the Costa Rican directives did not come to "complete fruition" because Costa Rica did not "wholly extinguish" the obligation of the Costa Rican banks to timely repay the foreign debt.¹⁶⁷ In *Braka*, however, the court focused on the terms of the depository contracts in determining that Mexico performed a *fait accompli* with respect to the effects of its exchange controls on the certificates of deposits in the case.¹⁶⁸ This *fait accompli* analysis stands in direct contrast with the test espoused in *Allied II*. Moreover the *Allied II* court concluded that Costa Rica could not "wholly extinguish" the obligation of its banks to timely repay their debts in United States dollars; in fact, however, the directives delayed payment of the debt. In sum, the *Allied II* and *Braka* decisions provide no guidelines for proper application of the *fait accompli* test.

In *Allied II*, the court also applied an "ordinary" situs test, although the court did not reveal the source of this test.¹⁶⁹ It is not apparent why

163. 764 F.2d at 1122-23. For a discussion of *Callejo*, see *supra* notes 88-95 and accompanying text.

164. 764 F.2d at 1123.

165. For a discussion of the *Garcia* approach to siting intangible property where an act of state question is raised, see *supra* notes 66-74 and accompanying text.

166. See *Tabacalera*, 392 F.2d at 715. For a discussion of the *fait accompli* test as developed in the *Tabacalera* case, see *supra* notes 57-65.

167. 757 F.2d at 521.

168. 762 F.2d at 224-25.

169. *Allied II*, 757 F.2d at 521-22. The *Allied II* court merely cited the *Taba-*

the court performed this test since the court deemed it inapplicable to its act of state analysis.¹⁷⁰ Under the "ordinary" situs test the *Allied II* court weighed the interests of the United States versus those of Costa Rica in siting the debt within its borders.¹⁷¹ The court found numerous United States interests, focusing on New York's status as a financial center and on the terms of the loan agreement under which the Costa Rican banks agreed to pay United States dollars in New York to the creditor banks and consented to jurisdiction in New York.¹⁷² In contrast, the court found that Costa Rica's "interest in the contracts at issue [was] essentially limited to the extent to which it [could] unilaterally alter the payment terms."¹⁷³

The court's balancing fell short in its consideration of Costa Rica's interest in siting the debt within its borders.¹⁷⁴ In *Allied II*, Costa Rica imposed directives temporarily restricting payment of external debt as a means to stabilize its economy in a time of economic crisis.¹⁷⁵ Costa Rica's interest in the effectiveness of these directives far exceeded its ability "to unilaterally alter the payment terms" of the foreign loan agreements.¹⁷⁶

In *Callejo*, the Fifth Circuit, after rejecting the *fait accompli* test, analyzed the "incidents of the debt" by focusing solely on the contractual terms of the certificates of deposit.¹⁷⁷ The court sited the deposits in Mexico because they were issued and payable in Mexico.¹⁷⁸ The *Callejo* court did not examine the interests and purposes behind the Mexican government actions in determining whether the act of state doctrine was applicable.¹⁷⁹

calera case for the proposition that siting intangible property for act of state purposes is different from ordinary purposes. *Id.* (citing *Tabacalera*, 392 F.2d at 715-16).

170. *Id.* at 521. The *Tabacalera* court did not identify a single ordinary situs test, but rather, pointed out that intangible property can be located in different places for different purposes, such as venue or tax purposes. 392 F.2d at 714-15.

171. 757 F.2d at 521-22.

172. *Id.* at 521.

173. *Id.* at 522.

174. One commentator has characterized the "ordinary" situs test employed by *Allied II* as a weighing of "apparent irrelevancies." See Letter to the Editor from David Lindskog, INT'L FIN. L. REV., May, 1985, at 24.

175. See *Allied II*, 757 F.2d at 519.

176. See Campbell, *Allied Bank's Effect on International Lending: A Non-US Perspective*, INT'L FIN. L. REV., Aug. 1985, at 26, 28-29. This commentator views the court's balancing process as a "fallacy" and observes that "[t]he holding of the Court of Appeals in *Allied II* amounts to a negative response to the question: may a foreign state ever expect that its acts will be given precedence over local obligations?" *Id.*

177. 762 F.2d 222. For a discussion of the *Callejo* case, see *supra* notes 88-95 and accompanying text.

178. 764 F.2d at 1124.

179. See *id.* The *Callejo* court enunciated several factors which are relevant

Allied II, *Braka*, and *Callejo* together illustrate that the situs approach is dysfunctional as a means to determine the applicability of the act of state doctrine to cases involving intangible property. Rather than engage in the fiction of locating intangible property, it is submitted that a court should examine the rationales underlying the act of state doctrine to determine its applicability.¹⁸⁰

Banco Nacional de Cuba v. Sabbatino stands as the most recent unified Supreme Court pronouncement on the proper application of the act of state doctrine.¹⁸¹ In *Sabbatino*, the Court enunciated two broad guidelines that a court should consider in deciding whether to apply the act of state doctrine. First, a court should determine whether there exists codification or consensus regarding some controlling legal principle which it can readily apply to resolve the litigation.¹⁸² Where no such codification or consensus exists, the *Sabbatino* Court concluded that application of the act of state doctrine is appropriate to protect a court from being faced with "the sensitive task of establishing a principle not inconsistent with the national interest or with international justice."¹⁸³ Second, a court should examine the importance of the implications of an issue for United States foreign relations; where an issue "touches sharply on national nerves" there arises strong justification for resolution of the issue exclusively by the political branches.¹⁸⁴ The *Sabbatino* Court added that, within these guidelines, a court should contrast "the practices of the political branch with the limitations of the judicial process."¹⁸⁵ The *Sabbatino* Court noted that the executive branch can engage in diplomacy to

under an "incidents of the debt" analysis, including the intent of the parties and the involvement of the American banking system. *Id.* at 1123-24. However, when the court applied the test, it relied solely on the fact that the certificates were issued and payable in Mexico. *Id.* at 1124.

The problem with the *Callejo* approach is that the dispositive factors in the court's decision to apply the act of state doctrine were the terms of the certificates of deposit. *Id.* The act of state doctrine, however, is rooted in separation of powers concerns; its application embodies a determination that a court will recognize the acts of foreign sovereign governments, *inter alia*, in deference to concerns of United States foreign policy. Accordingly, the terms of a contract between two private parties are inapposite to the issue of whether the doctrine should apply. For a discussion of the separation of powers rationale for the act of state doctrine, see *supra* notes 41-45 and accompanying text.

The act of state doctrine is a judicial doctrine and cannot be waived by an agreement between two parties. See RESTATEMENT (REVISED), *supra* note 19, § 469 comment e. It is submitted that where a court determines the applicability of the doctrine based on the terms of the contract at issue it is effectively allowing two parties to waive the doctrine based on the terms of their agreement.

180. For citations to authorities advocating this approach, see *supra* note 160.

181. 376 U.S. 398 (1964). For a discussion of the *Sabbatino* opinion, see *supra* notes 40-45 and accompanying text.

182. 376 U.S. at 428.

183. *Id.*

184. *Id.*

185. *Id.* at 431.

marshal the rights of all United States citizens who are harmed, whereas the judiciary can have only an occasional impact depending on a plaintiff's ability to initiate a lawsuit in the United States.¹⁸⁶ The *Sabbatino* Court observed that "[p]iecemeal dispositions of this sort involving the probability of affront to another state could seriously interfere with negotiations being carried on by the Executive Branch and might prevent or render less favorable the terms of an agreement that could otherwise be reached."¹⁸⁷

An analysis under the *Sabbatino* guidelines as applied to the facts of *Allied* mandates application of the act of state doctrine. First, as evidenced by the lack of consistency between the various opinions in the case, there is no codification or consensus regarding the controlling legal principles applicable to the issues raised in the *Allied* case.¹⁸⁸ Second, *Allied* implicates the debt crisis of the developing countries, which is most severe in Latin America, and surely qualifies as an issue with broad implications for United States foreign policy touching "sharply on national nerves."¹⁸⁹ The *Sabbatino* decision concluded that in deference to separation of powers concerns, a court has to weigh the competence of the judiciary versus that of the political branches in resolving act of state questions.¹⁹⁰ Against the background of the broad international implications of the Third World's debt burden, the *Allied II* court should have recognized that a comprehensive resolution will not emerge from deci-

186. *Id.* See also *First Nat'l City Bank*, 406 U.S. at 788 (Brennan, J., dissenting).

187. 376 U.S. at 432.

188. See Note, *supra* note 74, at 934-35 (noting absence of history of judicial management of international debt). See also Reisner, *Default by Foreign Sovereign Debtors: An Introductory Perspective*, 1982 U. ILL. L. REV. 1, 5-6 (while most debtor nations have had to restructure their external debt since 1981, there has been no litigation concerning sovereign defaults).

189. *Sabbatino*, 376 U.S. at 428. For a discussion of the Latin American debt and the involvement of United States banks, see *supra* notes 1-2 and accompanying text. The gravity of the problem was recently summarized by a leading political scientist:

It should not be downgraded or ignored. Not only is it a crushing burden on the Third World, but it severely injures the U.S. economy as well. Hundreds of thousands of jobs in export industries have been lost because of it. It represents serious dangers to American foreign policy and security interests. Relations with Latin American countries have already suffered, and much worse may come if the burden cannot be lifted. Hopeful beginnings of democracy may well be stifled, and suffering nations may well turn to anticapitalist and anti-U.S. solutions. It is to be hoped that bankers and financial authorities will demand only what they can reasonably expect to receive and permit the debtor countries to resume progress toward more abundance. And the financial system must be reformed to prevent another such breakdown in the future.

Wesson, *The Third World Debt*, in 51 VITAL SPEECHES OF THE DAY 619, 622 (1985).

190. 376 U.S. at 431.

sions by United States courts.¹⁹¹

The *Allied II* decision foreshadows the potentially adverse effects of piecemeal judicial decisions. In *Allied II*, the Costa Rican directives restricting external debt repayment were temporary.¹⁹² While the decision was pending in *Allied I*, the Costa Rican government, its central bank, and other Costa Rican state financial entities, including the defendants in *Allied*, signed a refinancing agreement with a United States bank that was acting as a coordinating agent for all of Costa Rica's external creditors.¹⁹³ Over 170 foreign creditors accepted the agreement, including all but one member of the Allied syndicate.¹⁹⁴ Fidelity Union Bank of New Jersey (Fidelity Union), which had the largest piece of Allied's loans,¹⁹⁵ refused to enter into the restructuring, and Allied Bank proceeded to press the appeal and subsequent rehearing for the benefit of Fidelity Union alone.¹⁹⁶

The *Allied II* case has set a precedent for "rogue creditors" such as Fidelity Union to disrupt sensitive international debt negotiations.¹⁹⁷ Large money-center banks cannot practically seek judicial relief for foreign loan defaults because their exposure is so large that their interests

191. See Lowenfeld, *Foreword*, 17 N.Y.U. J. INT'L L. & POL. 485, 491 (1985).

192. 757 F.2d at 519. For a discussion of the Costa Rican directives, see *supra* note 122.

193. See Brief of Defendants-Appellees at 12-14, *Allied II*, 757 F.2d 516 (on file at office of *Villanova Law Review*).

194. *Id.* at 13.

195. See Kallen, *supra* note 121, at 97. Fidelity Union invested \$2.3 million in the syndicate's \$10 million loan. *Id.*

196. 757 F.2d at 519.

197. The problem of a rogue creditor or windfall beneficiary was addressed by Justice Brennan in his dissenting opinion in *First Nat'l City Bank*. 406 U.S. at 794 (Brennan, J., dissenting). In that case, the petitioner sought to retain excess proceeds it realized by selling collateral in satisfaction of a loan made to a Cuban bank prior to its nationalization by Castro's government. *Id.* at 778-79 (Brennan, J., dissenting). The petitioner contended that it was equitably entitled to the excess to offset its losses incurred by Castro's expropriation of its property in Cuba. See *id.* Justice Brennan observed that the petitioner was seeking a windfall at the expense of other claimants. *Id.* at 794 (Brennan, J., dissenting). He explained:

Our Government has blocked Cuban assets in this country for possible use by the Foreign Claims Settlement Commission to compensate fairly all American nationals who have been harmed by Cuban expropriations. Although those assets are not now vested in the United States or authorized to be distributed to claimants, it is reasonable to assume that they will be if other efforts at settling claims with Cuba are unavailing. In that event, if petitioner prevails here, it will, in effect, have secured a preference over other claimants who were not so fortunate to have had Cuban assets within their reach and whose only relief is before the Claims Commission.

Id. It is suggested that the *Allied II* court should have foreseen the analogous and potentially detrimental consequences of a judgment in favor of Fidelity Union. For further discussion of *First Nat'l City Bank* case, see *supra* notes 108-18 and accompanying text.

have merged with the interests of the debtor countries in seeking revitalization of debtor country economies.¹⁹⁸ However, regional banks with less aggregate exposure generally have no long term commitment to the economic restoration of debtor nations and so will turn to the courts when their loans fall into default. Under the *Allied II* approach of siting the intangible property, courts can provide relief to these smaller banks without consideration of the larger implications on the international economy and on the aggregate of United States creditors.

The refusal of the *Allied II* court to recognize the validity of the act of state doctrine may reflect the court's unwillingness to set a precedent potentially undermining the sanctity of all United States loan agreements with debtor nations.¹⁹⁹ The court may have perceived that a judgment in favor of the Costa Rican bank debtors would signify approval of unilateral actions by debtor countries to restructure their private obligations. A judgment in favor of the United States creditor, on the other hand, could afford protection to United States creditors by deterring such unilateral actions. Analogous concerns were addressed by the Supreme Court in *Sabbatino* regarding expropriation made in violation of international law.²⁰⁰ The claimants in *Sabbatino* urged that "the economic pressure resulting from [not applying] the act of state doctrine will materially add to the protection of United States investors."²⁰¹ In response, the Court stated:

We are not convinced, even assuming the relevance of this contention. Expropriations take place for a variety of reasons, political and ideological as well as economic. When one considers the variety of means possessed by this country to make secure foreign investment, the persuasive or coercive effect of judicial invalidation of acts of expropriation dwindles in comparison. The newly independent states are in need of continuing foreign investment; the creation of a climate unfavorable to such investment by wholesale confiscations may well work to their long-run economic disadvantage. Foreign aid given to many of these countries provides a powerful lever in the hands of the political branches to ensure fair treatment of United States nationals. Ultimately the sanctions of economic embargo and the freezing of assets in this country may be employed. Any country willing to brave any or all of these consequences is unlikely to be deterred by sporadic judicial de-

198. See Meissner, *Crisis as an Opportunity for Change: A Commentary on the Debt Restructuring Process*, 17 N.Y.U. J. INT'L L. & POL. 613, 617-18 (1985) (large money-center banks are interested in assuring that debtor countries "have the opportunity to generate needed foreign exchange").

199. See Hoffman & Deming, *supra* note 160, at 506-09 (arguing that expectations of parties to international loan contracts should control).

200. 376 U.S. at 435-36.

201. *Id.* at 435.

cisions directly affecting only property brought to our shores. If the political branches are unwilling to exercise their ample powers to effect compensation, this reflects a judgment of the national interest which the judiciary would be ill-advised to undermine indirectly.²⁰²

This reasoning is equally compelling with respect to defaults by foreign debtors involved in loan transactions with United States banks. Debtor nations must remain creditworthy to revitalize their economies. External political and economic pressures from multilateral financing agencies such as the IMF and from the United States government can also be exerted to discourage debtor nations from taking unilateral actions affecting their debt. Finally, where a debtor nation takes unilateral action, the political branches, not the judiciary, have the means and power to negotiate a favorable and comprehensive resolution for all United States banks.²⁰³ It is submitted that piecemeal adjudication, the approach supported by the decision in *Allied II*, does not satisfactorily accommodate the rights of all interested parties, nor does it necessarily serve the foreign policy relations of the political branches.

B. Consistency With United States Law and the Bernstein Exception

In *Allied I*, the Second Circuit, rather than reviewing the act of state defense, held that "[c]omity considerations demand that the actions of Costa Rica be recognized in the courts of the United States," concluding that the Costa Rican directives were consistent with United States law and policy.²⁰⁴ Despite the widespread criticism of the *Allied I* analysis,²⁰⁵ vestiges of this approach resurfaced in *Allied II*.²⁰⁶ By interposing the question of whether the foreign act is consistent with United States law and policy before an act of state analysis, it is submitted that the *Allied II*

202. *Id.* at 435-36.

203. See, e.g., Comment, *supra* note 1, at 113-31. These commentators suggest an alternative to allowing unilateral suits against defaulting foreign banks. *Id.* at 113. The authors propose a response on the national level by the Executive, as was taken by President Carter during the Iranian hostage crisis with respect to an Iranian threat to withdraw its vast deposits from United States banks, rather than private suits against the foreign banks. *Id.*

204. *Allied I*, *supra* note 10, at 747. For a discussion of *Allied I*, in which the court found that the Costa Rican directives were consistent with United States law and policy, see *supra* notes 127-38 and accompanying text.

205. See, e.g., Ebenroth & Teitz, *supra* note 6, at 237-42 (criticizing novel use of comity as alternative to act of state doctrine and characterizing such alternative as "too flimsy" for such use); Tigert, *Allied Bank International: A United States Government Perspective*, 17 N.Y.U. J. INT'L L. & POL. 511, 523-24 (1985) (comity is only one factor to be considered in choice of law analysis); Zaitzeff & Kunz, *supra* note 49, at 473-74 (*Allied I* court relied on comity to avoid question of siting debt under act of state analysis).

206. In *Allied II*, the Second Circuit reversed its decision regarding comity and the consistency of the directives with United States law and policy before it examined the act of state defense. 757 F.2d at 519-20.

decision added a new and unnecessary layer of analysis to suits involving acts of a foreign state.

Prior to *Allied II*, the Second Circuit employed the law and policy analysis only as a *second step*, and then only if the court concluded that the act of state doctrine was inapplicable.²⁰⁷ In *Allied II*, however, the court reviewed the law and policy analysis before considering the act of state doctrine. Then, after concluding that the act of state doctrine was inapplicable, the court again considered whether the Costa Rican directives were consistent with United States law and policy. The court failed to explain why it went through this new procedure; therefore, it remains to be seen whether lower courts will follow this three-part approach.²⁰⁸

Unlike a "law and policy" analysis, the act of state doctrine involves separation of powers issues.²⁰⁹ Arguably, these issues are crucial when a case involves acts by a foreign sovereign, and it is suggested that it is improper to decide such cases without addressing separation of powers concerns. Moreover, there is no judicial economy in reviewing "law and policy" before the act of state. In fact, a "law and policy" analysis may be more confusing in its application than the act of state doctrine. In *Allied II*, for example, the court was not consistent with prior case law as it compared the Costa Rican directives to both United States domestic and foreign affairs law.²¹⁰

Additionally, there is a danger that creditors may read the *Allied II* decision as standing for the proposition that unilateral restructuring of private obligations is inconsistent with United States law and policy. In finding the Costa Rican directives inconsistent, the *Allied II* court relied

207. See, e.g., *Republic of Iraq v. First City Nat'l Bank*, 353 F.2d 47 (2d Cir. 1965), cert. denied, 382 U.S. 1027 (1966). For a discussion of the Second Circuit's "second step" analysis, see *supra* notes 96-100 and accompanying text.

208. It is possible that the court was only refuting its decision in *Allied I* before proceeding to its own analysis. However, the court did not definitely indicate that this was its approach. Thus, lower courts cannot be sure of the proper procedure for deciding act of state cases.

209. For a discussion of these separation of powers issues, see *supra* notes 40-45 and accompanying text.

210. See *Zaitzeff & Kunz*, *supra* note 49, at 461, 477. These commentators noted this further ambiguity in the *Allied* cases. In prior cases involving extraterritorial acts of state, the Second Circuit examined the consistency of the foreign law with United States public policy such as the United States domestic policy against confiscation of property. *Id.* at 461 (citing *Menendez v. Saks & Co.*, 485 F.2d 1355 (2d Cir. 1973), *rev'd on other grounds sub nom. Alfred Dunhill, Inc. v. Republic of Cuba*, 425 U.S. 682 (1976)). The *Allied I* court, however, relied at least in part on the consistency of the Costa Rican directives with United States foreign policy. *Zaitzeff & Kunz*, *supra* note 49, at 477. This ambiguity was perpetuated by the *Allied II* court, which deemed the Costa Rican directives inconsistent with United States foreign policy regarding international debt restructuring. *Allied II*, 757 F.2d at 519-20. Thus, even assuming the validity of a law and policy analysis set forth in the *Allied* opinions, it is not clear whether extraterritorial acts of state must be viewed as consistent with United States public policy or with its foreign policy.

exclusively on the assertion in the Government's amicus brief that the executive branch disfavored unilateral action by debtor countries and instead favored multinational cooperation within the framework of IMF procedures.²¹¹ It is arguable, however, that the directives were consistent with IMF procedures since the IMF later indicated approval of Costa Rica's actions.²¹² Neither the court nor the amicus brief addressed the IMF's approval of Costa Rica's actions. Thus, it is unclear at this point what degree of involvement with the IMF's system of international cooperation and negotiation is required for a sovereign's act of restructuring its debt to be consistent with United States law and policy.

While the Second Circuit in *Allied II* relied on the Government's brief for the "law and policy" question and not for the act of state doctrine, the criticisms of the *Bernstein* exception set forth by six Justices of the Supreme Court in *First National City Bank v. Banco Nacional de Cuba*²¹³ apply with equal force to *Allied II*. First, the issue of whether a court should recognize the validity of an act of a foreign sovereign government is a *judicial question*.²¹⁴ Such determinations should occur under a principled analysis of the act of state doctrine and should not be unduly influenced by executive suggestions which vary with political currents.²¹⁵ Further, the court's adherence to the executive's suggestions

211. See *Allied II*, 757 F.2d at 519-20. The executive department's brief stated:

There is thus a process in place for resolving economic adjustment problems such as Costa Rica's. It is a process that adequately balances the interests of creditors and debtors, public and private, generally in the framework of an IMF-approved adjustment program, and which relies for solutions on the voluntary cooperation of each. This process is impaired, not aided, by judicial recognition of a country's unilateral suspension of external payments on debts expressly made payable in the United States.

Brief for the United States as *Amicus Curiae* at 11-12, *Allied II*, 757 F.2d 516.

212. See Quale, *Allied Bank's Effect on International Lending: The New York Angle*, INT'L FIN. L. REV., Aug. 1985, at 26, 27. A special lending facility of the IMF provided additional funding for Costa Rica from 1981 through 1984 to help the country meet its debt service. See J. PIPPENGER, *supra* note 12, at 155-56. To obtain this funding, Costa Rica was required to submit to the IMF a detailed statement of its economic objectives and policies for the period of the loan, and Costa Rica obtained IMF approval of its objectives. *Id.*

213. 406 U.S. 759 (1972). For a discussion of the *Bernstein* exception to the act of state doctrine, see *supra* notes 101-20 and accompanying text. See also Quale, *supra* note 212, at 30 (*Allied II* court's deference to executive branch "appears to be a throw-back to the *Bernstein* exception").

See Note, *supra* note 74, at 917 & n.83. This commentator similarly criticizes *Allied II* for the court's reliance on the executive's amicus brief: "The Second Circuit's reversal concerning the consistency of the Costa Rican decrees with U.S. law and policy . . . suggests that it uncritically accepted the government's arguments. Such acquiescence to executive suggestion undermines the integrity of the decision-making process and politicizes the act of state determination." *Id.* at 917 n.84 (citations omitted).

214. See RESTATEMENT (REVISED), *supra* note 19, § 469 comment e.

215. See *First Nat'l City Bank*, 406 U.S. at 790-91 (Brennan, J., dissenting).

in *Allied II* demonstrates the court's failure to recognize potential latent effects of its decision that may be harmful to the conduct of United States foreign relations with Costa Rica.²¹⁶ To enforce its judgment, the United States creditor that prevailed in *Allied II* would be required to bring enforcement proceedings outside the United States as the Costa Rican bank defendants had no United States assets.²¹⁷ Presuming the creditor's success in such proceedings at some later date, enforcement could vex then current United States relations with Costa Rica. In a broader sense, given the political sensitivity of the developing world's debt crisis and its profound implications for United States economic vitality, a court must conscientiously avoid the risks of politicizing judicial decisions by undue deference to executive suggestions. An executive suggestion assures a court only that its adjudication of a foreign act of state will not embarrass the executive.²¹⁸ However, as Justice Brennan pointed out in his dissent in *First National City Bank*, embarrassment to the executive is only one policy consideration that a court should consider in deciding whether to recognize the validity of a foreign act of state.²¹⁹ The court should also consider whether there exists a consensus as to any controlling legal principles that might apply to the issue in the case, whether the issue has important foreign relations implications, and whether the judiciary is competent to serve the interests of all adversely affected parties. As was previously explained, these considerations in *Allied II* warrant judicial recognition of the sovereign's acts notwithstanding a contrary executive suggestion.²²⁰

VI. CONCLUSION

The act of state doctrine provides that a court shall not sit in judgment of the acts of a foreign sovereign government affecting property within that sovereign's dominion. Where a foreign sovereign act such as imposing currency controls affects international loan agreements or other financial transactions, the doctrine may emerge as the critical judi-

For a discussion of Justice Brennan's dissent, see *supra* notes 114-18 and accompanying text.

216. See *First National City Bank*, 406 U.S. at 792-93 (Brennan, J., dissenting). As Justice Brennan observed,

Resolution of so fundamental [an] issue (as the basic division of functions between the Executive and the Judicial Branches) cannot vary from day to day with the shifting winds at the State Department. Today, we are told, [judicial review of a foreign act of state] does not conflict with the national interest. Tomorrow it may.

Id. (quoting *Zschernig v. Miller*, 389 U.S. 429, 443 (1968) (Stewart, J., concurring)) (brackets by Justice Brennan).

217. See Ryan, *Defaults and Remedies Under International Bank Loan Agreements with Foreign Sovereign Borrowers—A New York Lawyer's Perspective*, 1982 U. ILL. L. REV. 89.

218. See *supra* notes 115-16 and accompanying text.

219. 376 U.S. at 785-90 (Brennan, J., dissenting).

220. See *supra* notes 188-91 and accompanying text.

cial principle in a United States court's decision to give or not give effect to the international agreement. In *Allied II*, the Second Circuit had to determine whether the act of state doctrine required the court to recognize the validity of Costa Rican directives that temporarily restricted the outflow of foreign currency, thereby compelling Costa Rican banks to default on a loan obligation to a United States banking syndicate.

The court's act of state analysis turned on an uncertain evaluation of the situs of the Costa Rican banks' debt. Where an act of state affects intangible property, courts, like the *Allied II* court, have attempted to determine the situs of the property since the act of state doctrine traditionally applies only to sovereign acts affecting property within a sovereign's borders. Courts have developed several analytically inconsistent situs tests, none of which function to serve the policy rationales underlying the act of state doctrine.

The act of state doctrine rests on the constitutional principle of separation of powers. Where a court is faced with an act of state involving intangible property, rather than attempt the fiction of siting the intangible property, the court should examine whether the policy rationales underlying the doctrine are implicated. If there exists no controlling legal principle to apply to the case and if the case involves sensitive issues of United States foreign affairs, a court should apply the doctrine and resolution of the issues in the case should be left to the political branches.

The *Allied* case arose in the broader context of the Third World debt crisis, which poses a serious threat to the economy of the United States and the world. The *Allied II* court's situs analysis does not provide a principled approach for future courts faced with these sensitive issues. An act of state analysis that adheres to the policies underlying the doctrine would provide more certainty for United States parties to international financial transactions and would better insure equality of treatment for all United States creditors and investors affected by the precarious economic status of the debtor countries.

In *Allied II*, the court stated that, based on international comity, it would recognize the validity of the Costa Rican directives if they were consistent with United States law and policy. The court performed this law and policy analysis before its act of state evaluation as a separate, alternate legal principle under which it could give effect to the Costa Rican directives. In so doing, the *Allied II* court added a novel and unnecessary layer of analysis. Additionally, the court was unduly influenced by advice from the executive that the Costa Rican directives were inconsistent with United States law and policy. The court should have relied directly on the act of state doctrine and made a judicial determination of its applicability. Such an approach would not be subject to executive pronouncements that vary with political currents.

M. Erin Kelly